No. 82-1766

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

SECURITIES INDUSTRY ASSOCIATION,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Respondents.

A. G. BECKER INCORPORATED,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOINT APPENDIX

[Counsel listed on inside cover]

PETITION FOR CERTIORARI FILED APRIL 29, 1983
CERTIORARI GRANTED OCTOBER 3, 1983

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Docket Entries in District Court,
Civil Action No. 80-2614

UNITED STATES DISTRICT COURT
DISTRICT OF COLUMBIA

Civ. A. No. 80-2614

A. G. BECKER INCORPORATED,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,

Defendants.

CAUSE

28 USC, 1331, 1332 and 1337. Action seeks a declaratory judgment that the defts. violated their statutory duty to administer, enforce & regulate the nation's banking system, etc.

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Docket Entries

DATE	*PROCEEDINGS*
1980	
Oct. 14	COMPLAINT: Exh. A; appearance
Oct. 14	SUMMONS (10) and copies (10) of complaint issued
Oct. 14	REQUEST by pltf. for appointment of special process server and ORDER by the Clerk appointing Mary Pelletter-Holzheimer to serve summons and complaint upon all defts.
Oct. 17	AFFIDAVIT OF SERVICE by Special Process Server Mary B. Pelletter-Holzheimer upon defts, #1 thru #8 on 10-14-80.
Dec. 11	MOTION by defts. for enlargement of time to answer or otherwise plead.
Dec. 16	ORDER filed 12-12-80 extending time to & including 1-5-81 for deft. to respond to the complaint. (N) JOYCE HENS GREEN, J.
Dec. 31	MOTION by defts. for enlargement of time in which to answer.
1981	
Jan. 9	ORDER filed 1-6-81 extending time to and including 1-19-81 for deft. to respond to complaint. (N) JOYCE HENS GREEN, J.
Jan. 12	NOTICE of defts. of filing certified copy of the administrative record; Administrative Record, Vol. I, Vol. 2.
Jan. 19	MOTION of defts. to dismiss or, in the alternative, for summary judgment, statement of material facts as to which there is no genuine issue, attachment, table of contents, table of authorities, exhibit A.
Jan. 19	MOTION of defts. to consolidate actions, memorandum of P&A, CA 80-2614 & CA 80-2730.

Docket Entries

DATE	*PROCEEDINGS*
Jan. 30	MOTION by pltf. for enlargement of time to respond to defts. motion to dismiss, memorandum of P&A.
Feb. 06	ORDER filed 2-4-81 that any motion to appear as amicus curiae be filed, accompanied with memorandum on the merits of this action within 10 days; pltf's reply to deft's motion to dismiss or for summary judgment no later than 2-27-81; There shall be no extensions. (N) JOYCE H. GREEN, J.
Feb. 10	ORDER filed 2-6-81 consolidating case with CA 80-2730 for hearing & trial of all matters. (N) JOYCE H. GREEN, J.
Feb. 12	MOTION of Securities & Exchange Commission for leave to file a memorandum of P&A Amicus Curiae, with respect to the defts' motion to dismiss or, in the alternative, for summary judgment and suggestion that the Court dispose of procedural issues before requiring briefs amicus curiae on the merits.
Feb. 17	MOTION by Goldman, Sachs & Co. for leave to file brief amicus curiae; Exhibit .
Feb. 23	ORDER filed 2-19-81 granting motion of Goldman, Sachs & Co. for leave to file brief amicus curiae. (N) GREEN, JOYCE HENS, J.
Feb. 23	MEMORANDUM of P&A's of Goldman, Sachs & Co. as Amicus Curiae in support of motion for summary judgment of pltf. Securities Industry Association, attachment.
Feb. 23	MEMORANDUM of Securities Industry Association in opposition to motion of Bankers Trust Co. for leave to appear as Amicus Curiae and to file a memorandum of law, exhibits A & B.

Docket Entries

DATE	*PROCEEDINGS*
Feb. 27	REPLY by Bankers Trust Co. as amicus curiae to memorandum of Securities Industry Association in opposition to motion of Bankers Trust Co. for leave to appear as amicus curiae & to file a memorandum of law, table of authorities.
Feb. 27	CROSS-MOTION by pltf. Securities Industry Association for summary judgment, statement of material facts, memorandum of P&A, table of contents, table of authorities, addendum.
Feb. 27	CROSS-MOTION by pltf. A.G. Becker, Inc. for summary judgment, memorandum of P&A, table of contents, appendix, statement of material facts as to which there is no genuine issue, affidavit of Thomas R. York, statement of material facts as to which there exists a genuine issue.
Feb. 27	MEMORANDUM by pltf. A.G. Becker, Inc. of P&A's in opposition to defts' motion to dismiss or, in the alternative, for summary judgment, table of contents, table of authorities.
Mar. 04	MEMORANDUM (corrected version) by pltf. of P&A's in support of pltf's cross-motion for summary judgment, table of contents, table of authorities, appendix.
Mar. 04	MEMORANDUM of pltf. (corrected version) of P&A's in opposition to defts' motion to dismiss or, in the alternative, for summary judgment, table of contents, table of authorities.
Mar. 04	ERRATA SHEET by pltf. to memorandum of P&A's of pltf's cross-motion for summary judgment.
Mar. 09	ORDER filed 3-5-81 granting motion of Securities & Exchange Comm. to appear Amicus Curiae and

Docket Entries

DATE	*PROCEEDINGS*
	allowing them to file memorandum re: motion of defts. to dismiss or for summary judgment; granting motion of Bankers Trust Company to appear as Amicus Curiae and accepting for filing Exhibit A. (N) JOYCE HENS GREEN, J.
Mar. 12	MOTION of defts. for enlargement of time to file a statement of P&A's in opposition to the cross-motions for summary judgment.
Mar. 17	ORDER filed 3-16-81 granting motion of defts. for enlargement of time until 4-21-81 to oppose pltf's cross-motion for summary judgment. (N) JOYCE H. GREEN, J.
Apr. 21	REPLY by defts. in support of defts' motion to dismiss or, in the alternative, for summary judgment, & opposition to pltfs. cross-motions for summary judgment, table of contents, table of authorities, exhibit 1, exhibit A, opposition to pltf. A.G. Becker Inc.'s statement of material facts as to which there is no genuine issue and opposition to pltf. Security Industry Assn.'s statement of material facts as to which there is no genuine issue.
Apr. 21	MEMORANDUM by Bankers Trust Co. of law as amicus curiae in opposition to pltfs' cross-motions for summary judgment & in further support of defts' motion to dismiss or, in the alternative, for summary judgment, table of contents, table of authorities, exhibit 1.
Apr. 23	MEMORANDUM BY PLTF. in opposition to motion of William Leighton for joinder as a party.
Apr. 23	OPPOSITION by defts. to motion for joinder of William Leighton, doing business as Option Advisory Service, Inc.

Docket Entries

DATE	*PROCEEDINGS*
May 08	REPLY MEMORANDUM by pltf. Securities Industry Association in opposition to defts' motion to dismiss, or for summary judgment & in support of its cross-motion for summary judgment, table of contents, table of authorities, exhibit.
May 08	REPLY BRIEF of amicus curiae Goldman, Sachs & Co.
May 12	MEMORANDUM by Securities & Exchange Commission as amicus curiae of P&A's, index, table of citations.
May 29	NOTICE by defts. of filing copies of a Policy Statement, attachment.
June 8	MEMORANDUM OF LAW by Amicus Curiae in opposition to the memorandum of Securities & Exchange Commission & in further support of defts' motion to dismiss or, in the alternative, for summary judgment, table of contents, table of authorities.
June 8	REPLY by defts. to memorandum of P&A's of the Securities & Exchange as amicus curiae.
June 12	RESPONSE by pltf. to defts' reply in support of defts' motion to dismiss or, in the alternative, for summary judgment, and opposition to pltfs. cross motions for summary judgment, table of contents, table of authorities, exhibits #1,2 & 3.
June 15	LETTER filed 6-12-81 dated 5-18-81 from Erick D. Roiter to Judge Green; corrected pages to P&A's of Commission (fiat) JOYCE H. GREEN, J.
Jun 18	MOTION of deft. to dismiss or for summary judgment and Motion of pltf. for summary judgment

Docket Entries

DATE	*PROCEEDINGS*
	argued and taken under advisement. (Rep: Bud Abramowitz) GREEN, J. JOYCE
July 29	ORDER filed 7-28-81 denying motion to William Leighton d/b/a Option Advisory Services to be joined as a party. (N) GREEN, JOYCE HENS, J.
July 29	MEMORANDUM OPINION filed 7-28-81. (N) GREEN, JOYCE HENS, J.
July 29	ORDER and judgment filed 7-28-81 for pltfs. A.G. Becker, Inc. and the Securities Industry Association and against defts. Board of Governors of the Federal Reserve System, Paul A. Volcker, Frederick H. Schultz, Nancy H. Teeters, J. Charles Partee, Henry C. Wallich, Emmett J. Rice and Lyle E. Gramley. (N) (See Order for details). GREEN, JOYCE HENS, J.
July 31	TRANSCRIPT of PROCEEDINGS, June 18, 1981; Rep: Barnet I. Abramowitz; Court Copy.
Sept 04	LETTER dated 8-21-81 from William Leighton, d/b/a Option Advisors Service, Inc. to Judge Green, "Let this be filed." (fiat) Joyce H. Green, J.
Sept 04	ORDER denying motion of William Leighton for relief from the Court's order of 7-28-81 denying movant joinder. (signed 9-3-81) (N) JOYCE H. GREEN, J.
Sep. 24	NOTICE OF APPEAL by William Leighton, d/b/a Option Advisory Services from order filed 7-28-81; $65.00 docketing fee and $5.00 filing fee paid & credited to U.S.; copies sent to Harvey L. Pitt, Richard M. Ashton.

Docket Entries

DATE	*PROCEEDINGS*
Oct. 01	COPIES of Notice of Appeal & docket entries transmitted to USCA. USCA# 81-2069.
Sep. 25	NOTICE OF APPEAL by defts. from order filed 7-28-81; No Fee-Govt.; copy sent to Harvey L. Pitt.
Oct. 01	COPIES of Notice of Appeal & docket entries transmitted to USCA. USCA# 81-2070.
Oct. 09	NOTICE OF CROSS APPEAL by pltf. from final judgment of 7-28-81; $65.00 docketing fee & $5.00 filing fee paid & credited to U.S.; copy sent to Richard M. Ashton and William H. Briggs, Jr., John W. Barnum, G. Duane Vieth, Edward G. Greene & John M. Lifton.
Oct. 09	COPIES of Cross Appeal & docket entries transmitted to USCA. USCA# 81-2096.
Nov. 17	RECORD ON APPEAL delivered to USCA, receipt acknowledged.
Dec. 28	COPY of Letter filed 12-22-81, dated 12-14-81 from William Leighton. (fiat) JOYCE GREEN, J. (orig. filed in CA 80-2730)
Dec. 28	COPY of Order filed 12-22-81 treating letter of 12-14-81 as motion to supplement record on appeal and granting said motion. (N) (orig. filed in CA 80-2730) JOYCE GREEN, J.
Dec. 28	COPY of Supplement to Record on Appeal filed 12-22-81. (orig. filed in CA 80-2730) JOYCE GREEN, J.
Dec. 29	SUPPLEMENTAL RECORD delivered. Receipt acknowledged.

Docket Entries in District Court,
Civil Action No. 80-2730

UNITED STATES DISTRICT COURT
DISTRICT OF COLUMBIA

Civ. A. No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,
Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,
Defendant.

CAUSE

DECLARATORY JUDGMENT AND INJUNCTIVE AND OTHER RELIEF
(12 U.S.C. 21 et seq.)

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Docket Entries

DATE	*PROCEEDINGS*
1980	
Oct. 24	COMPLAINT, appearance.
Oct. 24	REQUEST for order appointing special process server and order appointing Max L.C. Ratibor to serve summons and complaint on U.S. Attorney.
Oct. 24	SUMMONS (10) and copies (10) of complt. issued.
Oct. 29	NOTICE by defts. of related case (C.A. 80-2614).
Nov. 4	REASSIGNMENT of case from Judge Flannery to Judge Joyce Green.
Nov. 18	AFFIDAVIT of service (10) of service of summons and complaint on defts., Board of Governors of the Federal Reserve System, Benjamin R. Civiletti, Lyle E. Gramley, J. Charles Partee, Emmet J. Rice, Frederick H. Schultz, Nancy H. Teeters, Paul A. Volcker and Henry C. Wallich by certified mail; attachments.
Nov. 18	AFFIDAVIT of service of summons and complaint by special process server of service on M. Saulene Brown on 10/24/80.
Dec. 23	MOTION of defts. for enlargement of time to answer.
Dec. 31	MOTION of defts. for enlargement of time.
1981	
Jan. 6	ORDER extending time until and including 1/19/81 for deft. to answer. (N) GREEN, JOYCE J.
Jan. 12	NOTICE of filing by deft.; Administrative Record (2 Vols).
Jan. 19	MOTION of defts. to dismiss or, in the alternative, for summary judgment; statement of material facts; attachments; P&A's; Exhibit A.

Docket Entries

DATE	*PROCEEDINGS*
Jan. 19	MOTION of defts. to consolidate actions; P&A's.
Jan. 30	MOTION of Plif. for enlargement of time and setting of briefing schedule; memorandum.
Feb. 4	ORDER that motions to appear amicus curiae be filed accompanied with memorandum on the merits within 10 days; pltf's reply to motion to dismiss or for summary judgment to be filed no later than 2/27/81; there shall be no extensions. (N) GREEN, JOYCE J.
Feb. 9	ORDER filed 2-6-81 consolidating this case with 80-2614 for hearing and trial of all matters. (N) (filed in C.A. 80-2614) GREEN, JOYCE HENS, J.
Feb. 13	MOTION of Bankers Trust Company for leave to appear as Amicus Curiae and to file a memorandum of law; affidavit of John W. Barnum; Exhibit (memorandum).

Docket in Court of Appeals,
Civil Action No. 80-2258

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 80-2258

A. G. BECKER INCORPORATED,

Petitioner,

—v.—

THE BOARD OF GOVERNORS OF
THE FEDERAL RESERVE SYSTEM, et al.,

Respondents.

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Docket Entries

DATE	*FILINGS—PROCEEDINGS*
(V)10-14-80	4–Petitioner's petition for review of an order of the Board of Governors of the Federal Reserve System (m-14)
(V)10-15-80	Certified copy of petition for review was mailed to FRS
(T)11-24-80	Certified Index to Record (n-2)
(T)12-04-80	Corrected Certified Index to Record (n-2)
(T)12-04-80	4–Petitioner's motion to use deferred appendix procedure (m-4)
(T)12-24-80	4–Petitioner's motion to extend time to file brief (m-24)
(B)12-31-80	Clerk's order that counsel for the parties are granted leave to proceed under Rule 30(c), deferred appendix
(B)12-31-80	Clerk's order that petitioner's motion to extend time is granted and the time for filing petitioner's brief is extended for a period of thirty days after disposition of the pending motion to stay proceedings, should that motion be denied
(B)08-05-81	Clerk's order that the Clerk is directed to file petitioner's motion to stay proceeding and that the time for filing petitioner's brief and appendix is extended until thirty (30) days after final decision by the United States District Court for the District of Columbia in A.G. Becker Incorporated v. Board of Governors of the Federal Reserve System, Civil Action No. 80-2614. Counsel for petitioner shall advise the Court, through its Clerk, the status of the aforesaid Civil Action within ninety (90) days from the date of this order and, if necessary, and at ninety (90) day intervals thereafter

Docket Entries

DATE	*FILINGS—PROCEEDINGS*
(B)08-05-81	4-Petitioner's motion to stay proceedings—filed per above order
(T)08-17-81	1-Letter from counsel for petitioner advising of status
(V)08-18-81	4-Petitioner's motion to extend time to file brief for a 30 day period (m-18)
(B)08-31-81	Clerk's order that the time for filing petitioner's motion to govern the future course of this proceeding is extended to either thirty (30) days after appeals are docketed in this Court from the District Court's decision in Civil Action No. 80-2614 or thirty (30) days after the time for noting such appeals expires, whichever occurs first
(V)10-26-81	4-Petitioner's motion to consolidate action Nos. 80-2258, 81-1493, 81-2070 & 81-2096 and to establish briefing schedule (m-26)
(B)11-12-81	Clerk's order that Nos. 80-2258, 81-1493 and cross-appeals 81-12070 and 81-2096 are hereby consolidated
(V)11-27-81	Respondents' motion to consolidate appeal Nos. 80-2258, 81-1493, 81-2070, 81-2096 with appeal Nos. 80-2314 and 81-2058 (m-25)
(B)12-03-81	Clerk's order that Nos. 80-2258, et al. are hereby consolidated with Nos. 80-2314 and 81-2058

Docket in Court of Appeals,
Civil Action No. 80-2314

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 80-2314

SECURITIES INDUSTRY ASSOCIATION,
Petitioner,

—v.—

THE BOARD OF GOVERNORS OF
THE FEDERAL RESERVE SYSTEM, *et al.*,
Respondents.

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DATE	*FILINGS—PROCEEDINGS*
10-24-80	4–Petitioner's petition for review of an order of the Board of Governors of the Federal Reserve System (m-24)
10-29-80	Certified copy of petition for review was mailed to BD.GOV.FRS.
12-03-80	Certified Index to Record (n-2)
12-12-80	4–Petitioner's motion to defer filing of appendix, Rule 30(c) (m-12)
12-31-80	Clerk's order that counsel for the parties are granted leave to proceed under Rule 30(c), deferred appendix
01-02-81	4–Petitioner's motion to extend time to file brief to February 11, 1981 (m-2)
01-09-81	Clerk's order granting petitioner's motion to extend time to file brief to February 11, 1981
02-02-81	4–Petitioner's motion to stay proceedings (m-2)
02-02-81	4–Petitioner's motion to extend time to file brief (m-2)
02-19-81	Clerk's order granting petitioner's motion to extend time to file brief and the time for filing petitioner's brief is extended for a period of 30 days from the date of the disposition of the pending motion to stay proceedings

Docket Entries

DATE	*FILINGS—PROCEEDINGS*
03-13-81	Per Curiam order that petitioner's motion to stay proceedings is granted pending consideration of the motion to dismiss pending in Civil Action No. 80-2370 before the US District Court for the District of Columbia, provided that either party may at any time apply to this Court for removal of this stay. Counsel are directed to promptly notify this Court of final action by the District Court; MacKinnon, Wald (who did not participate) and Mikva, CJ's
08-07-81	Letter dated 08-07-81 from counsel for petitioner advising of status
08-14-81	Letter dated 08-13-81 from Clerk to counsel for petitioner requesting an appropriate motion to govern the future course of this proceeding
08-26-81	4-Petitioner's motion to defer briefing schedule and to establish time for filing future motion (m-26)
09-02-81	Clerk's order granting petitioner's motion to defer filing schedule and to establish time for filing future motion to and including 10/9/81
10-09-81	4-Petitioner's motion to consolidate appeal Nos. 80-2314 with 81-2058 (m-9)
10-21-81	Clerk's order granting motion to consolidate actions and that the briefing schedule be established in accordance with the rules governing the schedule in No. 81-2058; consolidated with No. 81-2058

Docket in Court of Appeals,
Civil Action No. 81-2058

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 81-2058

SECURITIES INDUSTRY ASSOCIATION,
Appellee,

—v.—

THE BOARD OF GOVERNORS OF
THE FEDERAL RESERVE SYSTEM, *et al.*,
Appellants.

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DATE	*FILINGS—PROCEEDINGS*
09-28-81	Copy of notice of appeal and docket entries from Clerk, District Court (n-8)
10-09-81	4–Appellee's motion to consolidate appeal Nos. 81-2058 and 80-2314 (m-9)
10-21-81	Clerk's order granting motion to consolidate actions and that the briefing schedule be established in accordance with the rules governing the schedule in No. 81-2058; consolidated with No. 80-2314
11-03-81	4–Appellee's motion to establish briefing schedule (m-3)
11-12-81	Certified Original Record (2 volumes); 2 volumes of administrative record (green covers) (n-8) (this is also the record in No. 81-2071)
11-12-81	Clerk's order that the motion to establish a briefing schedule is granted and a briefing schedule is set as follows: Forty (40) days from the date the record is docketed in 81-2058—Brief of

DATE	*FILINGS—PROCEEDINGS*
	the Board of Governors of the Federal Reserve System, et al., to be served and filed; Forty (40) days thereafter—Brief of the Securities Industry Association to be served and filed; Thirty (30) days thereafter—Brief of the Board of Governors of the Federal Reserve System, et al., to be served and filed; Fourteen (14) days thereafter—Reply brief, if any, of the Securities Industry Association to be served and filed. Subject to further order of the Court, the Clerk is directed to calendar the above cases for argument with Nos. 80-2258, et al., on the same day and before the same panel.
11-27-81	4-Appellants' motion to consolidate appeal Nos. 80-2258, 81-1493, 81-2070, 81-2096 with appeal Nos. 80-2314 and 81-2058 (m-25)
12-03-81	Clerk's order that Nos. 80-2258, et al. are hereby consolidated with Nos. 80-2314 and 81-2058

Docket in Court of Appeals,
Civil Action No. 81-2070

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 81-2070

A. G. BECKER INCORPORATED,
a Delaware Corporation,

Appellee,

—v.—

THE BOARD OF GOVERNORS OF
THE FEDERAL RESERVE SYSTEM, *et al.*,

Appellants.

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872-6988

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Docket Entries

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872-0013

DATE	*FILINGS—PROCEEDINGS*
10-01-81	Copy of notice of appeal and docket entries from Clerk, District Court (n-3)
10-26-81	4–Appellee's motion to consolidate actions Nos. 80-2258, 81-1493, 81-2070 & 81-2096 and to establish briefing schedule (m-26)
11-12-81	Clerk's order that Nos. 80-2258, 81-1493 and cross-appeals 81-2070 and 81-2096 are hereby consolidated; and that a briefing schedule is set as follows: Forty (40) days from the first filing of the records in Nos. 81-2058 or Nos. 81-2070 and 81-2096—Brief of the Board of Governors of the Federal Reserve System, et al., and any amicus curiae briefs in support of the Board to be served and filed; Forty (40) days thereafter—Brief of A.G. Becker, Inc. (not to exceed sixty (60) pages) and any amicus curiae briefs in support of Becker to be served and filed; Thirty (30) days thereafter—Brief of the Board of Governors of the Federal Reserve System, et al., to be served and filed; Fourteen (14) days thereafter—Reply brief, if any, of A.G. Becker, Inc. (not to exceed fifteen pages) to be served and filed. Subject to further order of the Court, the Clerk is directed to calendar these cases with Nos. 80-2314 and 81-2058 on the same day and before the same panel.

Docket Entries

DATE	*FILINGS—PROCEEDINGS*
11-18-81	Certified Original Record (2 volumes); 1 volume of transcript (under separate cover); and 2 volumes of administrative record (n-7) (This is also the record in 81-2069 and 81-2096)
11-27-81	4–Appellants' motion to consolidate appeal Nos. 80-2258, 81-1493, 81-2070, 81-2096 with appeal Nos. 80-2314 and 81-2058 (m-25)
12-03-81	Clerk's order that Nos. 80-2258, et al. are hereby consolidated with Nos. 80-2314 and 81-2058
12-10-81	4–Appellant's (BD.GOV.FRS.) motion to permit filing of deferred appendix (m-7)
12-11-81	4–Appellant's (BD.GOV.FRS.) motion to extend time to file brief to 01/21/82 (m-11)
12-15-81	4–Consent (styled Stipulation) of A. G. Becker, Inc. to the appearance of Bankers Trust Co. as amicus curiae (m-14)
12-16-81	Clerk's order granting parties leave to proceed under Rule 30(c), deferred appendix
01-05-82	4–Consent (Styled Stipulation) of Bd. Gov. FRS to the appearance of Bankers Trust Co. as amicus curiae (m-5)
01-21-82	1–Letter dated 12/17/81 from counsel for A.G. Becker, Inc. consenting to the filing of a brief on behalf of the New York Clearing House Assoc. as amicus curiae
01-21-82	1–Letter dated 12/18/81 from counsel for Securities Industry Assoc. consenting to a brief on behalf of the New York Clearing House Assoc. as amicus curiae

Docket Entries

DATE	*FILINGS—PROCEEDINGS*
01-21-82	1-Letter dated 12/17/81 from counsel for BD.GOV.FRS. consenting to the filing of a brief on behalf of the New York Clearing House Assoc. as amicus curiae
01-21-82	25-Brief of the New York Clearing House Association as amicus curiae (m-21)
01-21-82	Clerk's order granting appellant's (BD. GOV. FRS) motion to extend time to file brief to 1-21-82
01-22-82	4-Motion of Bankers Trust Company as amicus curiae for leave to participate in oral argument (m-22)
01-22-82	15-Amicus Curiae (Bankers Trust Co.) brief (m-22)
01-25-82	4-Brief of Board of Governors of FRS (m-21)
02-18-82	4-Stipulation of parties consenting to leave to Goldman, Sachs & Co. to file brief as amicus curiae
03-05-82	4-Brief of Securities Industry Association (p-5)
03-05-82	15-Appellee/cross-appellant/petitioner (A.G. Becker) brief (p-5)
03-05-82	15-Amicus curiae (Goldman) brief (p-5)
03-26-82	4-Appellants' motion to extend time to file brief to 04/09/82 (m-26)
04-05-82	Clerk's order that appellants' (BD.GOV.FRS.) motion to extend time to file reply brief is granted on condition that the reply brief be hand delivered for filing in the Clerk's office by the close of business (4:00 p.m.) on 04/09/82. No further enlargement will be granted.

Docket Entries

DATE	*FILINGS—PROCEEDINGS*
04-05-82	15-Reply brief of Bankers Trust Co. as amicus curiae (m-5)
04-09-82	4-Reply brief of Bd. of Gov. (m-8)
04-26-82	4-Reply brief of Securities Industry Assoc. (m-23)
04-26-82	15-Reply brief of A.G. Becker, Inc. (m-26)
04-30-82	7-Joint Appendix (m-30) (Vol. I & II)
05-07-82	15-Brief of A.G. Becker as appellee/cross-appellant/petitioner (m-7)
05-07-82	15-Reply brief of A.G. Becker as appellee/cross-appellant/petitioner (m-7)
05-13-82	15-Petitioner-Plaintiff-Appellee (Securities Industry Assoc.) brief (m-12)
05-13-82	15-Petitioner-Plaintiff-Appellee (Securities Industry Assoc.) reply brief (m-12)
05-14-82	15-Brief of Bd. of Gov. as appellants (m-14)
05-14-82	15-Reply brief of Bd. of Gov. as appellants/cross-appellees/respondents (m-14)
05-26-82	Clerk's order that the motion of Bankers Trust to participate in oral argument is denied and that the following times are allotted for oral argument: Board of Governors—20 minutes on direct appeal; Securities Industry—15 minutes; A.G. Becker—15 minutes; Board of Governors reply to direct appeal issues and response to cross-appeal issues—20 minutes; A.G. Becker reply—10 minutes
06-03-82	Argued before Tamm, CJ; Robb, SCJ; and Wilkey*, CJ

Docket Entries

DATE	FILINGS—PROCEEDINGS
11-02-82	Opinion for the Court filed by Circuit Judge Wilkey.
11-02-82	Dissenting opinion filed by Senior Circuit Judge Robb.
11-02-82	Judgment by this Court that the judgment of the District Court is reversed, in accordance with the opinion for the Court filed this date.
11-02-82	Mandate order.
11-02-82	Per Curiam order by the Court sua sponte that the dissenting opinion filed by Senior Circuit Judge Robb this date is hereby amended (see order for details)
11-16-82	1-Appellants' bill of costs (m-16)
12-17-82	15-Appellee/cross-appellant/petitioner (A.G. Becker) joint petition for rehearing and suggestions for rehearing en banc (m-17)
02-02-83	Per Curiam order that the joint petition for rehearing, filed 12/17/82, is denied; Tamm and Wilkey, CJs and SCJ Robb (who did not participate)
02-02-83	Per Curiam order, en banc, that the joint suggestion for rehearing en banc is denied; CJ Robinson, Wright, Tamm, MacKinnon, Wilkey, Wald, Mikva, Edwards, Ginsburg, Bork and Scalia, CJs (Circuit Judges MacKinnon and Mikva would grant the suggestion for rehearing en banc) (CJ Robinson and Circuit Judges Wald, Ginsburg and Bork did not participate in the foregoing order)

Docket Entries

DATE	*FILINGS—PROCEEDINGS*
02-14-83	Certified copy of opinion, judgment and order of 11-2-82 and bill of costs in the amount of $697.60 issued to BGFRS and district court.
02-22-83	Receipt dated 02-22-83 from Clerk, District Court for Certified Original Record 2 vols.; 1 vol. of transcript under separate cover and 2 vols. of administrative record
05-05-83	Notice from Clerk, Supreme Court that petition for writ of certiorari was filed on 04-29-83 in SC No. 82-1766
10-06-83	Letter dated 10-05-83 from Clerk, Supreme Court asking that the record be certified and transmitted to Supreme Court
10-11-83	Letter dated 10-07-83 from Chief Deputy Clerk transmitting record to the Supreme Court
10-12-83	Clerk's order that certiorari having been granted, the Clerk of the Supreme Court has requested the transmission of the record on appeal to that Court. Accordingly the Clerk of the District Court is requested to certify and return to this Court the record on appeal previously transmitted, and since returned, in Civil Actions 80-2175, 80-2614 and 80-2730
10-13-83	Receipt dated 10-13-83 from Clerk, Supreme Court for record

Letter, dated November 19, 1971, from Robert Bloom to Richard A. Nordbye

[Letterhead of The Administrator of National Banks]

November 19, 1971

Mr. Richard A. Nordbye
Vice President & General Counsel
First National Bank of Minneapolis
Minneapolis, Minnesota 55480

Dear Mr. Nordbye:

This is in response to your letter dated November 15, 1971 concerning the possibility of the bank's acting as a dealer in commercial paper. You ask three questions concerning the application of federal banking laws and regulations to the proposed service.

First, you inquire whether dealing in commercial paper would constitute dealing in securities prohibited by the Glass-Steagall Act, 12 U.S.C. 377, 378, 78 and 24. The answer to this question depends on whether note obligations commonly known as commercial paper are considered securities for this purpose. This office has taken the position that such obligations are not "securities" for the purposes of the Glass-Steagall Act, provided such notes are exempt from registration under Section 3(a)(3) of the Securities Act of 1933, and that a national bank may deal in such exempt securities.

Secondly, you ask whether we would consider commercial paper owned by the bank as investment securities not subject to the lending limits of the bank contained in 12 U.S.C. 84. The long-standing position of the office is that commercial paper are loan assets subject to the usual rules concerning loans to single interests.

Thirdly, you ask the legal effect of the bank undertaking to repurchase commercial paper which it sells. The existence of

Letter, dated November 19, 1971

such a repurchase obligation would constitute the transaction a borrowing by the selling bank subject to its over-all debt limit pursuant to 12 U.S.C. 82. See our Interpretive Ruling 7.7519.

I trust that the above is responsive to your inquiry.

Sincerely,

/s/ ROBERT BLOOM
Robert Bloom
Chief Counsel

Letter, dated February 24, 1972, from F. H. Ellis to Robert D. Armstrong

February 24, 1972

Mr. Robert D. Armstrong
Vice President
First National Bank of Memphis
P. O. Box 84
Memphis, Tennessee 38101

Dear Mr. Armstrong:

This will acknowledge receipt of your letter of December 23, 1971, addressed to Kenneth W. Leaf, Regional Administrator of National Banks in Memphis, Tennessee, which has been forwarded to this office for reply. The bank wishes to initiate a service whereby it would act as the broker for the commercial paper issued by some of the larger local companies. This service would be handled through the bank's government bond department in a manner similar to that now in use for commercial paper and government bill transactions. Under the subject proposal, the bank would receive an order from a customer for commercial paper, which would be transmitted to the issuing company. If the paper is available, the company will deliver notes to the bank for the account of the customer.

The subject proposal raises a possible legal question concerning the Glass-Steagall Act (12 U.S.C. 378) which is generally interpreted as prohibiting commercial banks from engaging in the business of dealing in securities. The question is whether commercial paper is to be considered securities for this purpose. The Act refers to "stocks, bonds, debentures, notes, or other securities." There is no definition in the act of "other securities." The Securities Act of 1933 and the Securities Exchange Act of 1934 which were under consideration by the Congress at the same time as the Glass-Steagall Act, contain very broad definitions of securities which do include evidences of debt such as commercial paper. However, as your letter points out, there is a statutory exemption from the registration

requirements of the Securities Acts for the debt obligations of business corporations provided that such obligations arise out of "current transactions" and have a maturity of nine months or less. (Sec. 3(a)(3).

The intention of the Congress in providing the Section 3(a)(3) exemption from registration requirements is consistent with the general purpose of the 1933 securities legislation which was to provide disclosure and protection for the general investing public. Commercial bodies such as banks, mercantile corporations, insurance companies, etc., were considered to be sophisticated in the making of investments without need of government protection in this area.

Although no court, to our knowledge, has ruled on the question, we believe it reasonable to conclude that since commercial paper is purchased almost exclusively by financially sophisticated institutions, there was no intention in Glass-Steagall to prohibit commercial banks from engaging in the brokerage or other aspects of buying and selling such notes. Additional persuasive reasons exist for this conclusion. What is commonly known as commercial paper are after all nothing but loans to industrial corporations, a type of transaction engaged in by banks every day. Indeed, the issuance by industrial corporations of commercial paper is so closely related to ordinary bank loan activity that recently several leading New York banks have abandoned the use of an independent prime rate for commercial loans and have instead adopted a moving rate directly tied to the market rate for commercial paper.

For the reasons expressed above, it is our opinion that there is no legal bar to general dealing in commercial paper by a national bank.

Very truly yours,

F. H. Ellis
Chief National Bank Examiner

Memorandum, dated October 27, 1978, from Neal L. Petersen to Mr. Loeser.

[Letterhead of Board of Governors of the Federal Reserve System]

Date 10-21

TO: Mr. Loeser

FROM: Neal L. Petersen

Re: BTCo. Commercial Paper

Per our discussion yesterday. The attached was given to me by Jim Boechle.

[handwritten note]

Attachment to Memorandum, dated October 27, 1978 from Neal L. Petersen to Mr. Loeser.

Bankers Trust Company ("BTCo") proposes to carry on three types of activity involving commercial paper ("CP"):

(1) *Direct issue of CP*—This activity consists of acting as agent for an issuer of CP. The issuer decides how much, at what rate and for what maturity it wants to sell CP. BTCo, acting as the issuer's agent, solicits orders for such CP and sells such CP to those offerees who are interested. BTCo may also do the mechanical issuance. This activity is not forbidden for purposes of Glass-Steagall Act as a bank is permitted "[t]he business of . . . selling . . . securities . . . without recourse, solely upon the order, and for the account of customers . . .". In fact, BTCo and many other banks have been carrying on this activity for some time.

(2) *Direct Issue of CP with financial advisory services*—This activity consists of acting as agent for and financial advisor to an issuer of CP. BTCo, acting as financial advisor to the issuer, checks the market for an issuer. BTCo then advises the issuer how much, at what rate and for what maturity it should sell CP. Then BTCo, acting as the issuer's agent, solicits orders for such CP and sells such CP to those offerees who are interested. BTCo may also do the mechanical issuance. From time to time, without prior commitment, BTCo may lend short-term funds to such issuer at or near the commercial paper rate, either on open account or taking back a note. So long as there is no commitment to place the CP, or to make a loan, both the financial advisor and lender roles are outside the Glass-Steagall Act.

(3) *Buy and Sell CP in Secondary Market*—BTCo proposes to buy and sell already issued CP in the secondary market. This is the same as "discounting and negotiating" any other type of promissory note and is treated in 12 USC 24 paragraph Seventh as an activity separate from "[t]he business of dealing in securities . . .". Thus, it is an approved activity, separate

and distinct from any activity regulated by the Glass-Steagall Act. In addition, the Glass-Steagall Act, 12 USC 24 paragraph Seventh and Part 1 of the Regulations of the Comptroller of the Currency allow a bank such as ourselves to invest in such securities within the general limits on "Type 111 securities" and we could thus buy and sell such CP as the purchase and sale of investment securities.

Although for purposes of the above discussion of these three activities, we have assumed that CP is a security within the meaning of the Glass-Steagall Act, we are not so conceding and nothing herein contained should be otherwise construed.

We wanted the Federal Reserve to be aware of these activities and our position that they are not forbidden by the Glass-Steagall Act.

Board Memorandum, dated November 14, 1978 to Files Re: Sale of Third Party Commercial Paper by a Commercial Bank.

Board of Governors of the
FEDERAL RESERVE SYSTEM

Office Correspondence Date November 14, 1978

Files

Subject: Sale of third-party commercial paper by a commercial bank.

From John Walker

On November 13, 1978, I called Mr. William Kroener (212-422-3400) of the firm of Davis Polk & Wardwell, New York, New York. Mr. Kroener had called earlier on November 13 to speak with Mr. Petersen. Mr. Kroener stated to me that his firm is advising a certain "nameless client" (most likely Morgan Guaranty) regarding commercial paper activities that would not be dissimilar from the activities presently engaged in by Bankers Trust Company ("BTCo"). Mr. Kroener quoted statements attributed to Mr. Petersen in *Corporate Financing Week* (October 30, 1978) (see attachment) and *Business International Money Report* (October 27, 1978), and he inquired as to the status of Board staff consideration of the commercial paper activities of BTCo. I stated that Board staff is considering the Glass-Steagall implications of the activity of BTCo in the sale of third-party commercial paper. Mr. Kroener inquired whether a decision would be made regarding the Glass-Steagall implications of such activity before the end of the year and I responded that I expected so. Mr. Kroener inquired whether a memorandum submitted to Board staff by his firm within two weeks would be timely and I stated that I expected so. I informed Mr. Kroener that counsel for a nonbank company might also submit a memorandum to Board staff regarding the sale of third-party commercial paper by a commercial bank.

Attachment

Excerpt from Corporate Financing Week, undated.

Corporate Financing Week

FED DECISION ON BANKERS TRUST COMMERCIAL PAPER SERVICE EXPECTED SOON. The question of whether the new service for placing a corporation's commercial paper initiated by Bankers Trust is lawful under Glass-Steagall may be answered shortly for banks regulated by the *Federal Reserve*. Fed general counsel *Neal Peterson* said he expected a decision "soon"—soon meaning in this case, he said, "closer to next week than the end of the year."

The Fed has been looking at the matter since it was learned that BT had placed $25 million of commercial paper for *American Can Co.* and about $70 million for *ITT Corp.* (CFW, 9/25, 10/2).

Peterson said one reason why the Fed now intends to act with some speed is that "we have received some [other] inquiries on this service" from banks interested in performing a parallel function. BT is a state member bank of the Reserve System, which brings it under the Reserve Board as regard the application of Glass-Steagall. At issue is whether the placement service violates Glass-Steagall's prohibition against commercial banks underwriting securities.

Board Memorandum, dated November 17, 1978, from Evelyn Hurley to Donald Kohn

Board of Governors of the
FEDERAL RESERVE SYSTEM

Office Correspondence — Date November 17, 1978

To Mr. Donald Kohn — Subject: The role of Bankers Trust in selling commercial paper

From Evelyn Hurley

In recent telephone conversations with David Skolnick, vice-president in charge of the financial advisory staff at Bankers Trust Co., we discussed the bank's role in placing commercial paper for several commercial paper issuers. Mr. Skolnick's staff is responsible for obtaining new commercial paper business as well as for selling the paper of the bank's current issuers.

Mr. Skolnick says that Bankers Trust acts as an agent/advisor to its commercial paper issuers, charging each issuer a fee for placing the paper based upon the amount of the client's paper sold by Bankers Trust during the year but not exceeding a certain stated amount. The paper is sold to the investor on a discount basis, as is customary in both the dealer and the direct commercial paper markets and the interest rate paid by the Bankers Trust issuer is determined by the rates offered in the dealer market that day for that particular quality and maturity of paper.

Contrary to reports in financial publications, Skolnick insists that Bankers Trust does not buy the paper of an issuer but merely acts as an agent to place the paper with an investor. If a portion of an issuer's paper is not sold during the trading day, Skolnick noted, Bankers Trust makes an overnight loan to the issuer using the unsold paper as collateral. The bank charges the same interest rates as the issuer would have paid if the

paper had been sold. Mr. Skolnick said only about two such loans had to be made and none had been made since mid-October. [MATERIAL DELETED] also continue to issue through their regular dealers, A. G. Becker and Co. and Lehman Commercial Paper Corp., respectively. Mr. Skolnick said that he ex- [MATERIAL DELETED] In addition, he is negotiating with several foreign firms that have never used the commercial paper market.

The Bankers Trust Co. representative said that he had heard that a Minneapolis bank also was placing paper for commercial paper issuers. However, he indicated that several New York banks were investigating the possibility of entering the commercial paper market as agent/advisors. He did not identify the banks.

I called Dick Gelson at the New York Federal Reserve Bank to ask if the published aggregate of total commercial paper outstanding included the outstandings of Bankers Trust. He said at present it did not. He indicated there would be a general review of all commercial paper sources next year and collection of data from Bankers Trust would be considered at that time.

Bankers Trust Company Solicitation Materials

BANKERS TRUST
RESPONDS TO YOUR
COMMERCIAL PAPER NEEDS

[Illustration]

BANKERS TRUST ADDRESSES
YOUR SHORT TERM
FINANCING NEEDS

The traditional function of wholesale banks has been to supply short-term working capital to credit-worthy companies. These banks would gather funds and relend them at a spread which would compensate them for assuming liquidity and credit risks. For some 30 years the funds took the form of demand and savings deposits. In the 1960's and especially the 1970's these funds changed in form from demand and savings deposits to mainly short term interest bearing obligations—CDs, Federal Funds, Eurodollars, commercial paper, etc. Bankers Trust, which was among the first to recognize the importance of this development, established the capability to gather funds directly from market sources at the lowest cost, while satisfying certain liquidity criteria. As the bank gained experience in obtaining funds in this fashion it became evident that increasing our liquidity through wider sales distribution of our paper also lowered our cost, and that altering maturities to offset the impact of anticipated changes in interest rates further lowered the cost.

Paralleling these changes in the banking industry, more and more corporations began to fund themselves at a lower rate through the commercial paper market. Bankers Trust believes that this development is secular and not cyclical in nature.

Consistent with our traditional role of supplying working capital to corporations, Bankers Trust has decided to offer to certain select commercial paper issuers our financial advisory expertise, which is the result of our large sales distribution and

our market-timing capability. Specifically, we propose to sell, as your agent, your commercial paper for a fee that is competitive with that of commercial paper dealers.

The Value of Expanded Commercial Paper Distribution

Our job is the same as yours—assuring a dependable supply of funds at the lowest cost. At Bankers Trust we have learned that the way to do this is to expand sales distribution. Such expansion puts you in contact with more segments of the market and enables you to stay in touch with pools of liquidity as they shift from one sector of the economy to another. Also, expanding the sales force will work to increase demand for your commercial paper. As investor coverage increases, your corporate name becomes more familiar to a broader group of potential purchasers. Thus, there are more sources to tap when an increase in funds is needed. By increasing the number of investors that buy your name, you are less dependent on the investor who demands more than the market justifies. Longer term, this results in a significant and permanent cost saving. The more investors reached, the more flexibility you have to execute funding strategies.

Why Bankers Trust Is The Best Choice To Expand Your Commercial Paper Sales Distribution

There is certainly some overlap between the investors your present dealer does business with and our own investor group. However, because of our size we talk to many investors that your dealer does not. Unlike the investment banks, whose main focus has always been on the long term markets, our sales distribution effort is aimed principally at the shorter term investor. In 1977 our dollar volume in short term market activities alone averaged $4 billion a day. This is four times the daily activity of the entire dealer commercial paper market,

and over six times the daily dollar volume of the New York Stock Exchange. Available market share data indicate that we have a major share of the government market, with over 6% of the institutional market (according to the Federal Reserve Bank, only three other Government dealers, Merrill Lynch, Salomon Brothers, and First Boston, have over 5% of this market).

We had 13% of the bankers acceptance market in 1977, a significant share among the 13 dealers. Bankers Trust has an average of $14 billion of short term purchased funds outstanding. Over time we have been able to raise funds more efficiently than our competitors and the cost of our commercial paper issuance is competitive with CIT, GMAC, and Montgomery Ward. (Exhibits attached).

The reason for our success in these areas is a unique in-house sales distribution system that has given us access to a very large, diverse group of investors. Unlike most banks, Bankers Trust reaches investors directly instead of relying upon brokers and dealers to distribute our obligations. Domestically we are in contact with over 3,000 institutional investors in a variety of economic sectors and geographic regions. We have a specialized money market sales force in New York and in an expanding regional office network (Los Angeles and Chicago at present). We have international money market sales capability in 12 locations worldwide. We are a major factor in the global dollar market. In addition to a specialized sales distribution system which rivals that of the dealers, because we are a bank we have 600 calling officers who are selling the total services of the bank every day on a global basis. We also have access to the retail investor through over 200 branch offices in New York State. Through our correspondent bank network we have extensive relationships with a large number of regional commercial banks.

Our unique sales distribution network means that as your financial advisor and agent we can expand your commercial paper sales in a way that our competitors (either bank or

dealer) cannot. Our own experience shows that this insures not only the availability of funds, but also a lower cost of funding over the longer term.

Other Benefits If Bankers Trust Sells Your Commercial Paper

Our continuous contact with the short term investor enables us to stay abreast of the latest market trends and opportunities. From time-to-time, and where appropriate, we can provide you with CP arbitrage opportunities. That is, you might use your ready access to the CP market to realize a positive return by investing in higher yielding instruments in other markets. The net effect would be to decrease your overall cost of issuance.

There are operational advantages to be gained by having Bankers Trust sell your CP. These are centralization and increased time for market access. For that CP which we sell, it would be possible to centralize all your CP operations. Not only would we sell your paper, but we could also execute note issuance, delivery and redemption. The entire process could be initiated by one phone call. Furthermore, when we sell your paper, the delivery cycle between bank and dealer is eliminated. This means we can provide you with access to the CP market over a longer period of the day than is possible with a dealer.

Finally, by having Bankers Trust sell your CP it would be possible to bring together all the components of your cash management system. At present, we can provide daily balance information and money transfer capabilities via the Cash Connector. Also, we can offer a wide product line of investment alternatives when you have excess cash. The missing link is CP. Now, by having us sell your CP, you can centralize your complete cash management operation, which will result in increased efficiency and control.

Solicitation Materials

SUMMARY

A principal goal of the corporate financial officer is insuring the availability of funds to the corporation at the lowest possible cost. With regard to commercial paper we believe that the best way to accomplish this is to expand your sales distribution. We speak from successful experience, since we are charged with the same responsibility at Bankers Trust. Our developed sales distribution network and market expertise has accomplished these same goals for us, and we can and will put them to work for you.

MARKET SECTOR LIQUIDITY SHIFTS

Open Market Paper*

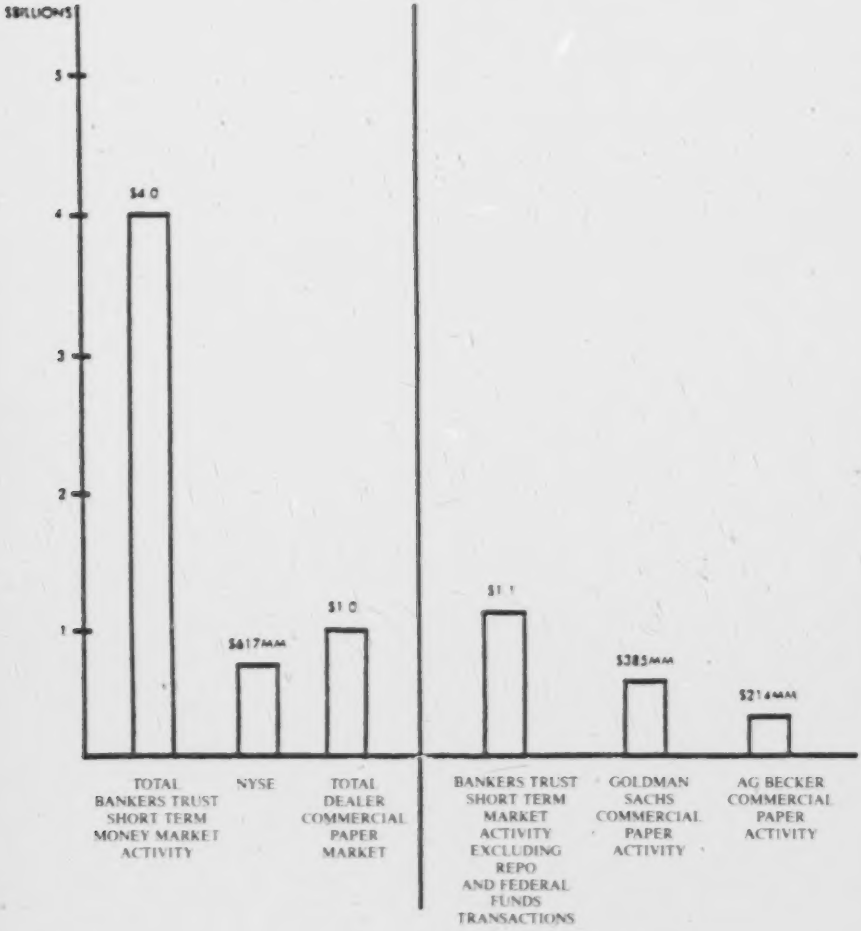
	1971	1972	1973	1974	1975	1976	1977	Projected 1978
Net Change in Open Market Paper	- .2	1.8	8.1	16.2	-1.5	8.1	14.8	12.0
Corporations	-2.3	1.4	6.5	- .6	4.3	2.2	10.3	4.0
Commercial Banks	.3	- .2	-1.3	2.2	1.1	3.7	1.8	.8
Thrifts	1.2	.4	- .6	—	.3	.9	.3	.3
Insurance Companies	.6	.3	1.6	2.8	- .9	- .7	1.2	1.0
Investment Companies	- .5	- .2	.2	.8	- .4	- .8	.4	.2
Foreign Investors	- .2	- .1	.3	6.6	-2.6	2.7	1.5	2.5
Individuals & Others	.7	.1	1.4	4.4	-3.4	.2	- .7	3.2

*Includes: Commercial Paper
Bankers Acceptances
Finance Bills

Source: Federal Reserve Bank of New York

Solicitation Materials

1977
DAILY VOLUME COMPARISONS



SOURCE: FEDERAL RESERVE DATA
ANNUAL REPORTS

Solicitation Materials

SHORT TERM INSTRUMENTS IN WHICH BANKERS TRUST IS A MAJOR FACTOR

- Federal Funds-Purchased/Sold
- Repurchase Agreements
- CD's-Primary/Secondary/Foreign
- Treasury Bills and Notes
- Bankers Acceptances-Domestic/Japanese
- BTNY Commercial Paper
- Eurodollar Time Deposits
- Eurodollar CD's-Primary/Secondary
- Tax Exempt Notes
- Federal Agency Securities

SHORT TERM MARKET PRESENCE

U.S. GOVERNMENT SECURITIES

- Bankers Trust does $385 million in daily volume of Treasury bills
- This is equivalent to a 6% share of the market
- We also have 6% of the total institutional market; the only other dealers with over 5% of this market are:

First Boston
Merrill Lynch
Salomon Brothers

BANKERS ACCEPTANCES

- In 1977, Bankers Trust had a 13% share of the market, or $12.5 billion annual volume
- This was achieved in competition with 13 other primary BA dealers
- We are one of only three banks recognized by the Federal Reserve as a BA dealer

Solicitation Materials

COMMERCIAL PAPER

- In 1977, total issuance of Bankers Trust amounted to $11 billion
- We accounted for 11% of the total bank holding company issuance
- In addition, we had $1 billion of issuance in the Canadian commercial paper market

FOREIGN MARKETS

- While the foreign markets are not yet a factor with regard to the domestic commercial paper market, this will change, given the evolving nature of the global dollar markets
- With $500 million daily volume in Nassau alone, Bankers Trust is already a factor in the global dollar market
  Bankers Trust has been a major force in the London market for 50 years

SHORT TERM MUNICIPAL NOTES

- In 1977, Bankers Trust was an underwriter of $2 billion
- This represents a 7% share of the short term municipal note market
- Bankers Trust managed 24 major, short term municipal underwritings

1977 COST OF COMMERCIAL PAPER FUNDING

	BANKERS TRUST	*GMAC*	*CIT*	*MONTGOMERY WARD*
Commercial Paper	5.50	5.58	5.96	5.48

Source: Annual Reports

DOMESTIC SALES DISTRIBUTION

- Expanding Sales Office Network
- Specialized Money Market Sales Force in New York, Chicago, Los Angeles
- Retail Branch Network in New York State
- National Account Officer Sales Force

Solicitation Materials

SHORT-TERM DOMESTIC DOLLAR VOLUME BY INDUSTRY

Corporations	50%
Banks & Trust Departments	24%
Insurance Companies	5%
State & Local Govts.	5%
Investment Companies	3%
Other	13%

SHORT-TERM DOLLAR VOLUME BY GEOGRAPHIC REGION

Northeast	50%
Midwest	24%
Southeast	14%
Southwest	7%
Far West	5%

FOREIGN SALES DISTRIBUTION

- Specialized Money Market Sales Capability in 12 International Money Centers
- Global Contact with the Short Term Investor Through 600 Account Offices Operating in Locations in 34 Countries

FOREIGN BRANCHES

London*	Milan*	Panama City*
Nassau*	Singapore*	Bahrain*
Paris*	Tokyo*	

FOREIGN SUBSIDIARIES

Belgium	Canada*	Korea
England*	Argentina	Malaysia
Germany*	Brazil	Thailand
Italy	Australia	Nigeria
Switzerland*	Hong Kong	Tunisia

Foreign Representative Offices in 13 Other Countries

*Location Has Specialized Money Market Sales Capability

POTENTIAL VALUE OF ARBITRAGE

1. ASSUME
   - A. Average CP outstanding $140MM
   - B. Cost of issuance* ..... ($140M)

2. THEN
   - A. Issue an additional ..... $10MM in CP—invest the proceeds at a positive spread of 50 basis points
     - a) Earnings $50M
     - b) Cost of Issuance ..... ($10M)

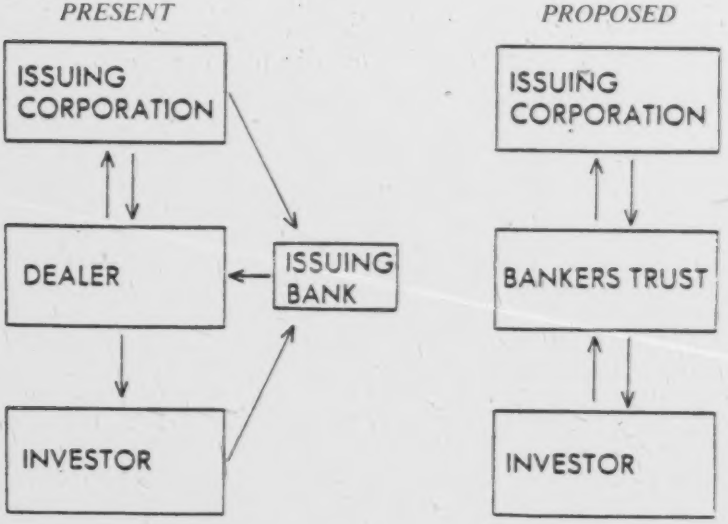
3. POTENTIAL VALUE OF ARBITRAGE
   - A. Total Outstanding $150MM
   - B. Total Cost of Issuance ..... ($150M)
   - C. Potential Earnings Value of Arbitrage $50M
   - D. Net Cost of Issuance ..... ($100M)
   - E. Net Cost of Issuance in Basis Points ..... 7BP's

*Assumes financial advisory fee of 10 BP's

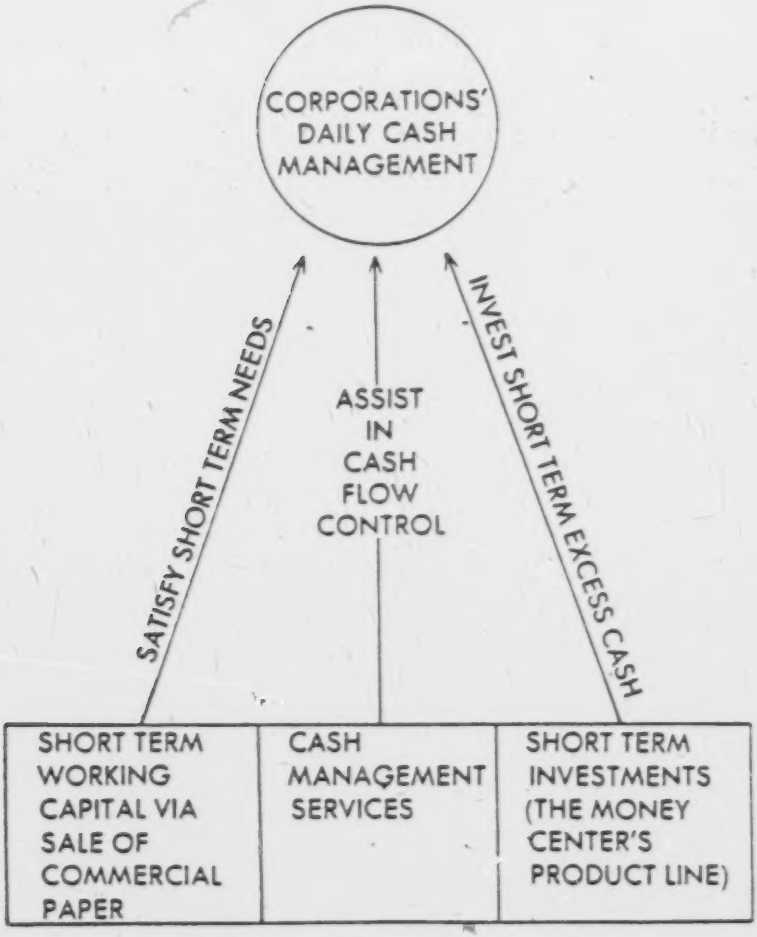
Solicitation Materials

CENTRALIZED COMMERCIAL PAPER OPERATIONS

- Elimination of Delivery Time: Issuing Bank To Dealer
- Control of Sales, Issuance, Delivery, Redemption in One Location
- Flexibility to Deal with Deadlines



COMPLETE CASH MANAGEMENT



BANKERS TRUST

MARKET SECTOR LIQUIDITY SHIFTS

Open Market Paper*

	1971	1972	1973	1974	1975	1976	1977	Projected 1978
Total Open Market Paper	- .2	1.8	8.1	16.2	-1.5	8.1	14.8	12.0
Corporations	-2.3	1.4	6.5	- .6	4.3	2.2	10.3	4.0
Banks	.3	- .2	-1.3	2.2	1.1	3.7	1.8	.8
Thrifts	1.2	.3	- .6	.2	.1	.9	.3	.3
Insurance Companies	.6	.3	1.6	2.8	- .9	- .7	1.2	1.0
Foreign Investors	- .2	- .1	.3	6.6	-2.6	2.7	1.5	2.5
Individuals & Others	.7	.1	1.4	4.4	-3.4	.2	- .7	3.2

*Includes: Commercial Paper
Bankers Acceptances
Finance Bills

Source: Federal Reserve Bank of New York

Letter, dated December 22, 1978, from James J. Baechle to Neal L. Petersen

[Letterhead of Bankers Trust Company]

December 22, 1978

Neal L. Petersen, Esq.
General Counsel
Board of Governors of the
Federal Reserve System
Constitution Avenue between
20th and 21st Streets, N.W.
Washington, D. C. 20551

Dear Mr. Petersen:

Thank you for your letter of November 22, 1978 concerning certain activities of Bankers Trust Company ("BTCo") in the sale of third party commercial paper ("CP"). In response to your questions concerning BTCo's activities, we are pleased to provide you with the following information:

(1) In acting as agent for and financial advisor to an issuer of CP, BTCo does not purchase the CP for its own account or for the account of customers (although BTCo does execute orders for customer directed investment).

(2) From time to time BTCo, without prior commitment, may lend short term funds (either its own or those of its parent holding company) at or near the commercial paper rate to those issuers for which it acts as agent and financial advisor, taking back notes, which subsequently may be sold, as evidence of indebtedness. In the case of such loans, BTCo observes established internal credit limits. These limits are consistent with the credit quality of the issuers involved, all of which are highly rated, credit worthy concerns. In any case, as a matter of policy the amount of such loans, taken together with all other loans to such issuer, may not be in excess of BTCo's legal lending limit to such issuer.

(3) BTCo does act as agent for its parent holding company in the solicitation of orders for and in the sale of commercial paper issued by the holding company. BTCo has engaged in such activity since the holding company began issuing commercial paper in 1969.

(4) BTCo does not place CP in accounts managed or advised by its trust department. Trust departments of banks with which BTCo maintains correspondent relationships may purchase CP from BTCo acting as agent for the issuer, just as those trust departments may purchase other high quality short-term investments from BTCo, such as Treasury bills, municipal notes, certificates of deposit and bankers acceptances. As with investment transactions with all customers, the amount of such business transacted is a function solely of BTCo's price and ability to satisfy the customer's investment requirements.

(5) BTCo, for its parent holding company, has purchased in the secondary market CP of issuers for which it acts as agent and financial advisor on four occasions. Some of the notes were sold prior to their maturity while the balance was held until maturity. In the case of such purchases, BTCo observes established internal credit limits. These limits are consistent with the credit quality of the issuer involved, all of which are highly rated, credit worthy concerns. In any case, as a matter of policy the amount of such purchases, taken together with all other loans to such issuer, may not be in excess of BTCo's legal lending limit to such issuer.

(6) BTCo sells CP to the same customers to whom it sells other short-term obligations such as Treasury bills, municipal notes, certificates of deposit and bankers acceptances. Such purchasers are located through an on-going extensive calling program on investors that have been identified as likely purchasers of short-term, high quality investments. The sources of that identification include contacts made by commercial lending officers of the bank, information gleaned from published statements of publicly held concerns, unsolicited telephone

calls by bank officers to investment officers of financial and non-financial institutions, and other conventional new business development techniques. BTCo does not maintain lists of commercial paper investors in conjunction with its role as paying agent for issuers of commercial paper. Normally, maturing commercial paper is submitted to a paying agent by an investor's clearing bank without mention of the actual investor. Although there is no numeric limit as such, BTCo does limit contacts for placement of CP to its base of institutional and other substantial purchasers of short-term investments. In the normal course of its business, BTCo does receive unsolicited calls from a small number of substantial individuals seeking short-term investment opportunities.

BTCo supplies all investors, prior to purchase, with a fact sheet on each issuer which provides general information on the issuer, including bond and commercial paper ratings and recent financial data. No representations are made to purchasers. No sale of CP by BTCo is subject to a repurchase agreement between BTCo and the purchaser.

(7) BTCo has spoken to several large credit-worthy corporations concerning the use of BTCo's CP services. The marketing effort is directed solely to highly rated issuers. Such solicitations are generally oral and in person, but a few have been written (samples enclosed). A brochure (copy enclosed) is generally left with prospective customers after each oral presentation. BTCo makes no commitments to the issuers. Prior to the inception of BTCo's CP financial advisory service, BTCo had in place advised lines of credit to most of the issuers which currently use BTCo's services. There has been no change in those lines in conjunction with those issuers using BTCo's CP services.

(8) Two directors of BTCo serve as directors of an issuer of CP for which BTCo acts as agent and financial advisor. William H. Moore is a director of both American Can Com-

pany and BTCo and William F. May is a director of both BTCo and American Can Company and is also Chairman of American Can Company. The CP business of American Can Company was solicited through financial officers. Messrs. Moore and May were not involved in the process of making the decision to use BTCo's CP services and were not even aware of the solicitation until American Can Company started to use the BTCo services.

(10) BTCo has not, at or about the time it commenced its CP services as agent and financial advisor, terminated the making of broker call loans or the extending of other types of credit to firms engaged in commercial paper sales activities. On the contrary, BTCo still extends substantial amounts of credit to firms engaged in CP sales activities.

BTCo does not have written agreements with issuers of CP for which it acts as agent and financial advisor (although it does have a written agreement if BTCo also performs the mechanical function of physically issuing CP, just as it does for issuers of CP which only use the physical issuance service and not the services of agent and financial advisor). You will find enclosed an analysis of the revenues associated with BTCo's CP services as well as a copy of the feasibility study relating to the services. As the CP services are highly integrated with other activities of BTCo's Money Market Center, it is not feasible to accurately determine the expenses that might be allocated to CP services as a "stand-alone" activity.

Due to the pressure of another matter, it has been impossible for us to complete a separate legal analysis within the time you desired a reply. In any case, we feel that our response makes clear that our activities are permissible. However, if after reading our response you have any further questions, either factual or legal, we would be most happy to respond to such questions.

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Letter, dated December 22, 1978

We regard your inquiry as part of the examination process and therefore your letter and this reply are confidential communications between us, and we hereby request that all such communications be kept confidential.

Sincerely yours,

(Signature illegible)

JJB/hb

Bankers Trust Company Solicitation Materials

July 6, 1978

Dear

Let me again thank you for spending your time and sharing your thoughts with us at our recent meeting. As you will remember, our discussion centered around the value of expanding the distribution of your commercial paper by having Bankers Trust act as a seller. Your suggestion was that, as a test of our ability, we receive an allocation of your paper to sell and then be measured on performance over a period of time, perhaps a year or so.

We would welcome this opportunity. In our opinion, an allocation of $10-$25 million would be suitable for this purpose, however there are a number of reasons why a larger (i.e. $25-$50 million) allocation is preferable:

1. Our performance in placing your paper is more fairly measured when larger amounts are sold. It may not be as relevant to compare our sales capability when smaller amounts (i.e. less than $10 million) are placed.

2. We are confident that our developed sales distribution system and the attention we will give you will generate savings for you over time. The larger the amount we sell the more meaningful and measurable the savings will be in absolute terms.

3. Most importantly, with a larger amount to sell, more of our customers will become acquainted with your name which, in essence, is our primary and mutual objective.

We are sincerely interested in serving by selling its commercial paper. If you have any questions, please let me know. In the meanwhile, I have asked to follow up with

Kindest regards.

Sincerely,

Executive Vice President

cc: Messrs.

60A

Solicitation Materials

[Letterhead of Bankers Trust Company]

July 25, 1978

Dear

Many thanks to you and for taking the time from your busy schedules to have lunch with us on Monday. We were pleased with your agreement concerning the advantages to be derived from expanded distribution and increased competition through the use of more than one commercial paper dealer.

Attached is our proposal to act as your agent to sell your commercial paper. Given that should continue to experience an increasing need for commerical paper, it makes sense to expand the distribution of your commercial paper with the addition of another selling agent. For those reasons outlined in the attached proposal, Bankers Trust is ideally and uniquely suited to provide that expanded distribution.

Very truly yours,

Senior Vice President

Enclosure

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Solicitation Materials

COMMERCIAL PAPER PROPOSAL

BANKERS TRUST ADDRESSES
YOUR SHORT TERM
FINANCING NEEDS

The traditional function of wholesale banks has been to supply short-term working capital to credit-worthy companies. These banks would gather funds and relend them at a spread which would compensate them for assuming liquidity and credit risks. For some 30 years the funds took the form of demand and savings deposits. In the 1960's and especially the 1970's these funds changed in form from demand and savings deposits to mainly short term interest bearing obligations—CD's, Federal Funds, Eurodollars, commercial paper, etc. Bankers Trust, which was among the first to recognize the importance of this development, established the capability to gather funds directly from market sources at the lowest cost, while satisfying certain liquidity criteria. As the bank gained experience in obtaining funds in this fashion it became evident that increasing our liquidity through wider sales distribution of our paper also lowered our cost, and that altering maturities to offset the impact of anticipated changes in interest rates further lowered the cost.

Paralleling these changes in the banking industry, more and more corporations began to fund themselves at a lower rate through the commercial paper market. Bankers Trust believes that this development is secular and not cyclical in nature.

Consistent with our traditional role of supplying working capital to corporations, Bankers Trust has decided to offer to certain select commercial paper issuers our financial advisory expertise, which is the result of our large sales distribution and our market-timing capability. Specifically, we propose to act as your agent, (along with A G Becker and Merrill Lynch) to sell your commercial paper for a fee that is competitive with that of the other dealers.

Solicitation Materials

THE VALUE OF EXPANDED
COMMERCIAL PAPER DISTRIBUTION

Our job is the same as yours—assuring a dependable supply of funds at the lowest cost. At Bankers Trust we have learned that the way to do this is to expand sales distribution. Such expansion puts you in contact with more segments of the market and enables you to stay in touch with pools of liquidity as they shift from one sector of the economy to another. Also, expanding the sales force through the addition of another selling agent will work to increase demand for your commercial paper. As investor coverage increases, you are able to access a broader group of potential purchasers. Thus, there are more sources to tap when an increase in funds is needed. By increasing the number of investors that buy your name, you are less dependent on the investor who demands more than the market justifies. Longer term, this results in a significant and permanent cost saving. The more investors reached, the more flexibility you have to execute funding strategies.

WHY BANKERS TRUST IS THE BEST CHOICE
TO EXPAND YOUR COMMERCIAL
PAPER SALES DISTRIBUTION

There is certainly some overlap between the investors you present dealers do business with and our own investor group. However, because of our size we talk to many investors that your dealers do not. Unlike the investment banks, whose main focus has always been on the long term markets, our sales distribution effort is aimed principally at the shorter term investor. In 1977 our dollar volume in short term market activities alone averaged $4 billion a day. This is four times the daily activity of the entire dealer commercial paper market, and over six times the daily dollar volume of the New York Stock Exchange. Available market share data indicate that we have a major share of the government market, with over 6% of the institutional market (according to the Federal Reserve

Bank, only three other Government dealers, Merrill Lynch, Salomon Brothers, and First Boston, have over 5% of this market).

We had 13% of the bankers acceptance market in 1977, a significant share among the 13 dealers. Bankers Trust has an average of $14 billion of short term purchased funds outstanding. Over time we have been able to raise funds more efficiently than our competitors and the cost of our commercial paper issuance is competitive with CIT, GMAC, and Montgomery Ward.

The reason for our success in these areas is a unique inhouse sales distribution system that has given us access to a very large, diverse group of investors. Unlike most banks, Bankers Trust reaches investors directly instead of relying upon brokers and dealers to distribute our obligations. Domestically we are in contact with over 3,000 institutional investors in a variety of economic sectors and geographic regions. We have a specialized money market sales force in New York and in an expanding regional office network (Los Angeles and Chicago at present). We have international money market sales capability in 12 locations worldwide. We are a major factor in the global dollar market. In addition to a specialized sales distribution system which rivals that of the dealers, because we are a bank we have 600 calling officers who are selling the total services of the bank every day on a global basis. We also have access to the retail investor through over 200 branch offices in New York State. Through our correspondent bank network we have extensive relationships with a large number of regional commercial banks.

Our unique sales distribution network means that as your financial advisor and agent we can expand your commercial paper sales in a way that our competitors (either bank or dealer) cannot. Our own experience shows that this insures not only the availability of funds, but also a lower cost of funding over the longer term.

Solicitation Materials

SUMMARY

A principal goal of the corporate financial officer is insuring the availability of funds to the corporation at the lowest possible cost. With regard to commercial paper we believe that the best way to accomplish this is to continue to expand your sales distribution as your needs for commercial paper continue to increase. We speak from successful experience, since we are charged with the same responsibility at Bankers Trust. Our developed sales distribution network and market expertise has accomplished these same goals for us, and we can and will put them to work for you.

Solicitation Materials

[Letterhead of Bankers Trust Company]

November 3, 1978

Dear Mr.

and I recently spoke about your meeting with . As the topic of commercial paper was discussed, has asked me to send you a letter outlining the operational procedures and our fee structures.

We would be prepared to act as one of your agents and financial advisors in the distribution of commercial paper. With our ability to distribute short-term money market securities, Bankers Trust is readily suited to help meet its short-term working capital requirements through the placement of commercial paper with investors, However, in those rare occasions in which we would be unable to satisfy all of requirements through the placement of paper with investors, we may, from time-to-time and without prior commitment, lend money at the commercial paper rate and take back a commercial paper note. We feel that this policy permits Bankers Trust to be completely competitive in providing with the short-term working capital it needs at the best possible price.

Our fee structure is also designed to keep Bankers Trust competitive. Our aim is not to attract business by cutting price but rather to offer a quality service at a fair price. Therefore, we would propose a rate schedule based on daily average outstandings as follows: .10% per annum on the first 100 million, .075% per annum on the next $100 million and .05% per annum above $200 million. The financial advisory fee would be calculated on a 360-day year, rather than a 365-day year.

The financial advisory fee is certainly an element in the total cost of placing commercial paper. However, in analyzing all the components of the cost of commercial paper, an issuer should bear in mind that the breakdown is roughly as follows: 9.25%

to the investor, plus .93% to pay for the back-up lines (assumes 10% compensating balances), plus .10% financial advisory fee.

Clearly, the largest component is that rate paid to the investor. By having two selling groups placing commercial paper, there will be an increase in the total market awareness of paper. This will lead to an increase in demand for the paper, and over time, will result in a lower average rate paid to the investor.

With regard to the mechanical aspects of note issuance, delivery and redemption, Bankers Trust offers a quality service at very competitive terms. We charge $6 per note issued and 65¢ per note for redemption.

As we discussed during our meeting in September, there is value in having Bankers Trust both place your notes with investors and provide the issuance of those notes. The value is derived from the fact that it streamlines your operations (the delivery cycle between the dealer and bank is eliminated) and allows us to be in the market one and one-half hours longer on your behalf. Nevertheless, while there is value in having Bankers Trust both issue commercial paper as well as place your paper with investors, it should be made clear that we are certainly capable of placing the commercial paper without providing the issuance service. In other words, if does decide to employ Bankers Trust on a trial basis in order to ascertain the benefits of broader distribution and competition, it would be possible to do so without having us also provide the note issuance.

I would like to reiterate Bankers Trust's interest in participating in · commercial paper activity. We have the demonstrated expertise in the short-term markets. Because we are a bank, we are the short-term money market experts. All we would ask for is the opportunity to demonstrate our capabilities. One suggestion in which this could be done would be to give us $25-50 million of commercial paper to place on

a trial basis (6 mos. to one year for example). During this period, we would hold the financial advisory fee in escrow. If at the end of that trial period the cost of the commercial paper we raised was greater than that of the competition, (assuming comparable maturities), we would refund the difference out of the financial advisory fees held in escrow. What would be receiving, at no risk, would be the chance to learn first hand about the value of competition and increased distribution.

We at Bankers Trust would look forward to discussing this subject with you at greater length and in more detail. If you have any plans to be in New York we would ask that you include us in your schedule. In the meantime, we would hope to see you again in . If there are any questions, please do not hesitate to give me a call at (212) 775 or send me a telex at 426955.

Sincerely,

Vice President

/dl

Solicitation Materials

November 21, 1978

Dear

It was good talking to you again last week. I am happy to see that continues to be so successful, due, I'm sure, in no small part to the efforts you have contributed. I was also pleased to hear that the possibility exists, after years of being a lender of funds, that might be a borrower of funds via commercial paper. Toward that end, I have enclosed some information you may find interesting on commercial paper. I have included some general historical articles about the commercial paper market, an article complementary to our efforts, as well as some check-lists of the information required by the rating agencies.

As we discussed, probably the most important consideration in entering the commercial paper market is having the top ratings. As a strong "AA" credit with a well known name, and a large market share this should not be a difficult step. We have contacts in the commercial paper rating areas of each of the three rating agencies and would be most happy to either provide the introductions or do whatever else you may deem appropriate if you should desire to initiate the rating process.

Besides having the top rating, a successful commercial paper funding operation is best achieved through having the broadest possible distribution. This is accomplished by using more than one selling agent. As you are aware, while there is a great deal of overlap, no one agent can possibly do business with all short-term money market investors. By using more than one selling agent, the money market access for paper is broadened. This should lead to an increase in demand for paper and, over time, this will result in a reduced cost of funding.

The other benefit to be derived from using more than one selling agent is competition. With competition, it is possible to have an objective standard of comparison against which to

measure performances over time. There is no other area of your business which is not characterized by some degree of competition. There is no reason why a commercial paper funding operation should be any different.

As you are aware, Bankers Trust Company has recently become an agent and financial advisor in the distribution of commercial paper. Thus far we are acting on behalf of . Because we are a large bank as well as a significant factor in the short-term money markets, we feel we can make a contribution to this business. Unlike the investment bankers, whose concentration has always been on the long-term markets, Bankers Trust, with over $14 billion in short-term liabilities is necessarily a short-term money market expert. Unlike other money center banks who are more apt to rely on others (ie dealers) to fund their short-term needs, Bankers Trust has a highly specialized short-term money market sales force which concentrates on reaching the end investors. Since we can do the issuance, delivery and redemption of commercial paper, these are operational advantages to be gained by using us to place commercial paper.

I could probably wax enthusiastically for two more pages about the advantages of Bankers Trust versus other money center banks and other dealers. Very simply, however, the argument is that, if should decide to enter the commercial paper market, there are some strong reasons why it would pay to have more than one selling agent. Further, there are strong reasons why one of those selling agents should be Bankers Trust. To that end I would look forward to seeing you at any time in or in New York to discuss this topic in more depth and in more detail.

Sincerely,

Vice President

/dl
enc.

Excerpt from memorandum, dated January 31, 1979, from the Securities Industry Association to the Board

Potential Hazards of Banks Distributing Commercial Paper

The SIA believes Bankers Trust's activities constitute such a clear violation of sections 16 and 21 of the Glass-Steagall Act that no analysis of the public policy objectives of the Act is necessary or even useful as a guide to its construction. Nevertheless, it can readily be demonstrated that many of the potential hazards cited by the Supreme Court in *Investment Company Institute* v. *Camp** are present in the distribution by a bank of commercial paper. The most obvious of these potential abuses relevant to commercial paper sales are:

(1) The investment by a bank of its own assets in frozen or otherwise imprudent securities investments.

Whenever Bankers Trust is unable to place an issue of paper successfully it, in effect, buys the remainder for its own account. This could mean a significant allocation of its assets to the credit of issuers whose paper is the most difficult to place, *i.e.*, those whose credit is least acceptable to buyers of commercial paper. Thus, the liquidity and prudence of such paper as an investment may be questionable.

(2) The exposure of a bank to promotional and other pressures, such as to make its credit facilities more fully available to those companies whose securities the bank has distributed.

Where a commercial paper issuer finds itself in unexpected financial difficulty, the bank which placed its paper may feel obligated to extend a loan that might not otherwise conform to its normal credit standards to avoid possible embarrassment and damage to its reputation among the investors who had purchased the paper. In other instances, a bank may decide, in the face of threat-

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* 401 U.S. 617 (1971).

ened litigation by the investor under the securities laws, that it is in the bank's best interest to provide a loan to help the issuer over its financial problems. Although a bank undoubtedly would not lower its lending standards merely to earn commercial paper fees, it might feel that, after the fact, either damage to its standing in the financial community or potential legal liability could justify a shading of its normal requirements.

(3) The incurring by bank depositors of losses on investments they have purchased in reliance upon the bank's reputation.

Although Bankers Trust describes its prospective market for commercial paper as consisting largely of institutions and "substantial" individuals, it was noted above that in the promotional material made available Bankers Trust touted its "access to the retail investor through over 200 branch offices in New York State." Clearly, this suggests depositors are not considered off limits as prospective purchasers of commercial paper; thus, depositors will be exposed to the risk of loss on their investments purchased through Bankers Trust.

(4) The use by banks of their reputations for prudence and restraint in selling securities.

Bankers Trust states in its December 22 letter that it sells commercial paper to the same investors to whom it sells other short-term obligations, such as Treasury bills, municipal notes, certificates of deposit and bankers acceptances. Surely there is a distinction in credit between the issuers of instruments such as these (the Federal government, municipal governments and banks) and the issuers of commercial paper. Yet by lending its name to the paper it sells, Bankers Trust may be implying that it regards the risks as comparable in its banking judgment.

Excerpt from memorandum, dated January 31, 1979

(5) The danger that banks might make loans to investors to facilitate the purchase of securities being distributed by the bank.

The information made available to us indicates no reason why Bankers Trust could not make loans to finance purchases of commercial paper.

(6) The obvious conflict between the promotional interests of the investment banker and the obligation of the commercial banker to render disinterested investment advice.

This conflict can take the banker out of his accustomed role and give him a pecuniary interest in recommending particular investments to persons who regard his advice as independent and objective. The conflict of course would be exacerbated in a situation where a bank were distributing commercial paper on behalf of an issuer which planned to use the proceeds of the sale to retire or pay down its indebtedness to the bank.

Many of these hazards may seem remote so long as Bankers Trust is distributing commercial paper of solvent, blue chip issuers. The Board undoubtedly recalls, though, that in recent history the commercial paper and other debt obligations of what were thought to be some of the nation's best-established credits have been demonstrated to be much riskier than imagined and, in some cases, virtually worthless.*

* * *

While the policies underlying the Glass-Steagall Act compel the conclusion that Bankers Trust's commercial paper activities constitute a violation of that Act, we believe it is unnecessary for the Board to engage in a "hazards" analysis of the present facts. The Board's job is not to decide whether bank under-

* See *e.g.*, "The Financial Collapse of the Penn Central Company", *Staff Report of the Securities and Exchange Commission* (August, 1972); "Transactions in Securities of the City of New York", *Securities and Exchange Commission Staff Report* (August, 1977).

writing of securities still presents risks to the economy and the banking system; that task was performed in 1933 by Congress. Until Congress acts to amend the judgment it then made, the Board's role is simply to apply that judgment to the present facts.

As demonstrated by the foregoing discussion of the legal issues, that task in this case is straightforward. Commercial paper clearly is a security for purposes of both sections 16 and 21. Section 16 prohibits

Excerpts from letter, dated February 2, 1979, from James J. Baechle to Neal L. Petersen

[Letterhead of Bankers Trust Company]

February 2, 1979

Neal L. Petersen, Esq.
General Counsel
Board of Governors of the
Federal Reserve System
Constitution Avenue between
20th and 21st Streets, N.W.
Washington, D.C. 20551

Dear Mr. Petersen:

Further to my letter of December 22, 1978 concerning certain activities of Bankers Trust Company ("BTCo") in the sale of third party commercial paper, and as requested in your letter of November 22, 1978, I am submitting an analysis of factual and legal considerations leading to the conclusion that BTCo's commercial paper activity is part of its traditional banking function of assisting corporations in financing their short term needs and not a violation of the Glass-Steagall Act.[1]

I. *Background*

Commercial paper is a well accepted means for corporations to raise funds for current business transactions through the issuance of short term promissory notes.[2] Because commercial paper notes are unsecured and bear only the obligation of the borrower, the market has been generally dominated by large corporations with impeccable credit ratings.[3] Historically banks were the largest purchasers of commercial paper[4] but in recent times they have been joined by other substantial investors, mostly institutional investors and other corporations.

In addition to their commercial paper purchases, commercial banks have traditionally advised and assisted corporate customers (including issuers of commercial paper) in obtaining

Excerpts from letter, dated February 2, 1979

[Material omitted in printing.]

In fact, a piece of commercial paper (which by law must be short term) is indistinguishable in substance from a note taken by a commercial bank to evidence a traditional short-term loan. Thus, there are no unknowns in the commercial paper markets.

BTCo's commercial paper activity, as outlined below, is nothing more than a continuation of the traditional activities of commercial banks, as outlined above.

II. *BTCo's Commercial Paper Activity*

The activity consists of acting as financial adivsor to and agent for an issuer of commercial paper. BTCo, acting as financial advisor to the issuer, checks the market for the issuer. BTCo then advises the issuer how much, at what rate and for what maturity it should sell commercial paper. Then BTCo, acting as the issuer's agent, sells such commercial paper to those who are interested. BTCo also may do the mechanical issuance.

BTCo makes no commitments to the issuers to place any amount of commercial paper. From time to time BTCo, without prior commitment, may lend short term funds at or near the commercial paper rate to those issuers for which it acts as agent and financial advisor, taking back notes, which subsequently may be sold, as evidence of indebtedness. In the case of such loans, BTCo observes established internal credit limits. These limits are consistent with the credit quality of the issuers involved, all of which are highly rated, credit worthy concerns. In any case, as a matter of policy the amount of such loans, taken together with all other loans to such issuer, may not be in excess of BTCo's legal lending limit to such issuer.

On occasion BTCo may purchase in the secondary market commercial paper of issuers for which it acts as agent and financial advisor. Some of the notes may be sold prior to their maturity while others may be held until maturity. In the case of

Excerpts from letter, dated February 2, 1979

such purchases, BTCo observes established internal credit limits. These limits are consistent with the credit quality of the issuer involved, all of which are highly rated, credit worthy concerns. In any case, as a matter of policy the amount of such purchases, taken together with all loans to such issuer, may not be in excess of BTCo's legal lending limit to such issuer.

BTCo supplies all investors, prior to purchase, with a fact sheet on each issuer which provides general information on the issuer, including bond and commercial paper ratings and recent published financial data. No representations are made to purchasers. No sale of commercial paper by BTCo is subject to a repurchase agreement between BTCo and the purchaser.

Please refer to my letter of December 22, 1978 for information on our marketing efforts or other details of our program.

III. *Commercial Paper and the Glass-Steagall Act*

The Comptroller of the Currency has long permitted national banks to act as dealers in commercial paper on the grounds that note obligations commonly known as commercial paper are not considered securities for the purposes of the Glass-Steagall Act. Thus, on November 19, 1971, the then Chief Counsel of the Comptroller of the Currency wrote to an inquiring national bank:

> ". . .you inquire whether dealing in commercial paper would constitute dealing in securities prohibited by the Glass-Steagall Act, 12 U.S.C. 377, 378, 78 and 24. The answer to this question depends on whether note obligations commonly known as commercial paper are considered securities for this purpose. This office has taken the position that such obligations are not 'securities' for the purposes of the Glass-Steagall Act, provided such notes are exempt from registration under Section 3(a)(3) of the Securities Act of 1933, and that a national bank may deal in such exempt securities.". . .and. . ."The long-stand-

ing position of the office is that commercial paper are loan assets. . ."[9]

We understand from the national bank recipient of that letter that the activity permitted has been carried on successfully and without incident, notice or ill-effect for approximately seven years.

As set forth in the preceding sections, we too find commercial paper indistinguishable from an ordinary short term commercial bank loan evidenced by a note and therefore we

[Material deleted.]

Letter, dated April 20, 1979, from Ralph C. Ferrara to Neal Petersen

[Letterhead of SECURITIES AND EXCHANGE COMMISSION]

April 20, 1979

Neal L. Petersen, Esq.
General Counsel
Board of Governors of the
Federal Reserve System
Washington, D.C. 20551

Dear Neal:

This responds to your letter of April 12, 1979, and the two enclosures (a draft letter to Bankers Trust Company, and a draft position paper of the Board's Legal Division entitled "Bank Commercial Paper Activities: An Interpretation of the Glass-Steagall Act") regarding the offer and sale by Bankers Trust Company of commercial paper issued by certain corporations. We appreciate very much the opportunity to share our thoughts with you before your position is announced formally. As we discussed on the phone, given your strict time schedule, it was not possible to evaluate comprehensively your draft letter and position paper. For the same reason, our comments have not been formally reviewed by the Commission. However, if your proposed letter and position paper come before the Board of Governors, we would appreciate an opportunity to present a more comprehensive analysis after Commission review.

As you know, the Commission has a continuing interest in the securities-related activities of commercial banks. In its 1977 Bank Study, for example, the Commission compared the regulation of broker-dealers with the regulation of similar securities activities of banks.[1] And, the Commission has a special interest

1 Securities and Exchange Commission, *Reports on Banks Securities Activities, Pursuant to Section 11A(e) of the Securities Exchange Act*

in the sale of commercial paper because of the recent problems surrounding the sale of commercial paper by Penn Central Company.[2] The Commission's report on the financial collapse of Penn Central described the adverse impact on investors when Penn Central went into bankruptcy with $40 billion of its "prime" commercial paper outstanding.

At the outset, however, we wish to emphasize that our interest is not in the traditional lending activities of banks whereby a commercial bank takes a note from an issuer as documentation of a lending agreement. Where a commercial bank lends money in exchange for the issuer's note, the type of Glass-Steagall questions with which your paper deals do not arise, even if these notes are popularly called commercial paper. By contrast, as we understand Bankers Trust Company's commercial paper activities, it offers and sells paper issued by major corporations to purchasers throughout the country. In the Bankers Trust Company situation, the ultimate lender is not the commercial bank; rather, the commercial bank's role is that of underwriter, distributor and/or dealer in commercial paper to a third party.

With respect to Banker Trust's activities, we have three main points. First, we question whether the word "security" in the Glass-Steagall Act should be limited, contrary to the plain words of the statute, to "investment security" or "speculative security." Second, we suggest that a more appropriate approach would be to apply the definition of "security" in the Securities Act to the Glass-Steagall Act, since the Acts were

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of 1934, Senate Comm. on Banking, Housing and Urban Affairs, 95th Cong., 1st Sess. (Comm. Print 1977).

2 *Staff Report of the Securities and Exchange Commission to the Special Subcomm. on Investigation of the Home Comm. on Interstate and Foreign Commerce, The Financial Collapse of the Penn Central Company* (Subcomm. Print 1972) [hereinafter cited as "*Penn Central Report*"].

passed within three weeks of each other. Third, we believe that the application of the definition of "security" from the Securities Act to Bankers Trust's activities would comport with the objectives of Congress in passing the Glass-Steagall Act.

To begin with, the staff's position paper asserts that the term "security" as used in Sections 16 and 21 of the Glass-Steagall Act (12 U.S.C. 24 ¶ 7 and 378) means an obligation "of the kind that is commonly known as an investment security," or is otherwise "predominantly speculative in nature." But this assertion appears to be contrary to both the language and the legislative history of the Glass-Steagall Act. With respect to the distinction between investment and non-investment securities, Section 16 of the Act broadly prohibits banks from dealing in or underwriting "securities and stock." By contrast, Congress chose the narrower term "investment securities" to describe what types of securities banks could purchase for their own account. Although Section 16 as passed in 1933 used the term "investment securities" in defining the scope of the prohibition against bank dealing or underwriting, the 1935 amendments broadened the language to its current extent, thus establishing that Congress specifically did *not* intend to limit the prohibition against bank dealing or underwriting to "investment" securities.[3]

Moreover, the staff's position paper does not set forth persuasive support for its conclusion that the determination as to whether obligations are "securities" should hinge on whether they are more or less speculative. While it is clear that the Glass-Steagall Act was in part a response to concern about speculation in securities, the position paper does not demonstrate that Congress intended that the prohibition against dealing or underwriting would apply only with respect to

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3 The 1935 amendment to Section 16 made it consistent with Section 21, which, as originally passed in 1933, prohibited a dealer or underwriter in "stocks, bonds, debentures, notes, or other securities" from also engaging in the business of commercial banking.

highly speculative securities. The legislative history of the Glass-Steagall Act which is cited consists of general statements which are inadequate authority in the absence of direct commentary on Sections 16 and 21.

The staff position paper places reliance on three items from the legislative history of the Act as passed in 1933 in support of its position that an obligation must be speculative to be a "security"—a passage in Senate Resolution 71 concerning the scope of the hearings ordered by Congress with respect to the nation's banking system, the preamble to the Act, and a Senate Report on the Act. The passage in Senate Resolution 71 concerning the scope of the hearings on the national banking system does not provide evidence that only highly speculative bank securities activities were considered within the scope of the hearings. Nor do the statements in the preamble to the Act and in the Senate Report suggest that Congress intended to make a distinction between more and less extreme cases of bank abuses, or to elevate the degree of speculativeness to a test for the applicability of Sections 16 and 21. In addition, the staff interpretation relies on the Board's 1933 letters to Congress concerning legislation which eventually became the Securities Act of 1933 for the proposition that commercial paper is not a "security" for purposes of the Glass-Steagall Act. The Board's position with respect to the treatment of commercial paper for purposes of securities regulation seems irrelevant, however, since, as discussed below, the Securities Act as subsequently passed treats such paper as securities.

Instead of focusing on "investment security" or "speculative security" through a selective reading of the legislative history of the Glass-Steagall Act, we believe that the proper inquiry is whether the commercial paper distributed by Bankers Trust is a "security" as that term was understood by Congress in 1933. Although Congress did not define "security" in the Glass-Steagall Act, it did define this term in the Securities Act,[4]

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4 Section 2(1) of the Securities Act of 1933, 15 U.S.C. 77b(1).

which was enacted only a few weeks earlier. The Senate Committee on Banking and Currency had responsibility for, and conducted extensive hearings concerning, both pieces of legislation. Because of Congress' concurrent consideration of these bills, the Securities Act definition of "security" should be used in defining "security" under the Glass-Steagall Act. Indeed, the staff of the Federal Reserve Board has recently concluded that where securities-related terms were defined in the Securities Act, and not defined in the Glass-Steagall Act, Congress intended the Securities Act definition to apply to the Glass-Steagall Act.[5]

Section 2(1) of the Securities Act defines a "security" to include any "note" or "evidence of indebtedness." Since the commercial paper distributed by Bankers Trust is clearly a "note" and an "evidence of indebtedness", it is a "security", and therefore subject to the antifraud provisions of the Securities Act.[6] While the definition of a "security" in Section 2(1) is prefaced by the phrase "unless the context otherwise requires", this phrase has been interpreted to exclude only commercial paper used in mercantile transactions and not for investment purposes.[7] And, a party asserting that any note is not a

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5 *See* Federal Reserve Board Staff, *Commercial Bank Private Placement Activities* (1977). In discussing the meaning of the word "issue" for purposes of the Glass-Steagall Act, the staff stated: "It is unlikely that Congress intended to give a content to the term as used in Glass-Steagall different from that given to the term in the Securities Act of 1933, which was enacted less than three weeks earlier." *Id.* at 87 n.6. The staff further stated that although the Securities Act definition of "underwriter" is not binding for Glass-Steagall purposes, "in view of the fact that Glass-Steagall was enacted only a few weeks after the Securities Act, Congress' use of the same terms in the two measures suggests that the Securities Act is a compelling analogy." *Id.* at 89.

6 Securities Act of 1933, Section 12(2), 15 U.S.C. 77*l*(2); Sections 17(a), (c), 15 U.S.C. 78q(a), (c).

7 *See, e.g., C.N.S. Enterprises, Inc.* v. *G & G Enterprises, Inc.*, 508 F.2d 1354 (7th Cir.), *cert. denied*, 423 U.S. 825 (1975); *McClure* v. *First*

"security" under the Securities Act has the burden of establishing that "the context otherwise requires."[8] As Bankers Trust's promotional literature illustrates, it is selling commercial paper of corporations to investors seeking to maximize short-term profits. Bankers Trust has not met the burden of showing that it is selling these notes in the type of purely commercial transactions that would justify removing the notes from the protection of the Securities Act.

Our view is reinforced by the legislative history of Section 3(a)(3) of the Securities Act,[9] which exempts from the registration requirements of that Act[10]—but not from its antifraud provisions—"any note *** which arises out of a current transaction or the proceeds of which have been or are to be used for current transactions, and which has a maturity at the time of issuance of not exceeding nine months ***." The original draft of the bill that became the Securities Act of 1933 provided no exemption from registration for short-term commercial paper.[11] The Section 3(a)(3) exemption evolved as a result of the comments and testimony of several parties, including the Federal Reserve Board, during the committee hearings on this draft. These parties argued that an exemption from the registration requirements was warranted because many businesses

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Nat'l Bank, 497 F.2d 490 (5th Cir. 1974); *Lino* v. *City Investing Co.*, 487 F.2d 689 (3d Cir. 1973). These cases construed the identical phrase preceding the definition of "security" in Section 3 of the Securities Exchange Act, 15 U.S.C. 78c(10).

8 *Exchange Nat'l Bank* v. *Touche, Ross & Co.*, 544 F.2d 1126, 1138 (2d Cir. 1976).

9 15 U.S.C. 77c(a)(3).

10 Securities Act of 1933, Section 5, 15 U.S.C. 77e.

11 *See Hearings on H.R. 4314 Before the House Comm. on Interstate and Foreign Comm.*, 73d Cong., 1st Sess. 179 [hereinafter cited as *Hearings on H.R. 4314*] (statement of William C. Breed).

issued short-term commercial paper to finance current operational business expenditures of a seasonal or periodic nature, and that to require registration in these circumstances would be unduly burdensome.[12] In response to these comments, Congress in Section 3(a)(3) carved out a subcategory of "notes" that would be exempt from the registration requirements, but Congress did not alter the basic definition of "security". In other words, "notes" that qualify for the exemption from registration still fall within the definition of "security," and are therefore subject to the antifraud provisions of the Securities Act. Thus, even if the commercial paper that Bankers Trust is distributing does qualify for the Section 3(a)(3) exemption from the registration requirements, as it asserts,[13] this paper is still a "security" for purposes of the Securities Act.

Moreover, we have serious questions about whether the securities distributed by Bankers Trust qualify for the exemption from registration in Section 3(a)(3) of the Securities Act. The Commission has enunciated four criteria that must be present before commercial paper will qualify for the exemption.[14] The paper must be:

(1) prime quality paper;
(2) not ordinarily purchased by the general public;
(3) issued to facilitate well-recognized types of current operational business transactions; and
(4) eligible for discounting at Federal Reserve banks.

Based on the information that has been furnished to the Commission, it is unclear whether the commercial paper being

12 *Id.* at 179-83; *Hearings on S. 875 Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. 94-95, 120 (1933).

13 *See* Letter from James J. Baechle, Senior Vice President and General Counsel, Bankers Trust Co., to Neal L. Petersen, General Counsel, Board of Governors of the Federal Reserve System (Feb. 2, 1979).

14 Securities Act Release No. 4412 (Sept. 20, 1961).

sold by Bankers Trust has met all four criteria necessary for an exemption from registration.[15] For example, it appears that Bankers Trust is selling commercial paper to the general public, and thus has not complied with the second requirement of the Release. Bankers Trust advertises to prospective clients that it has "access to the retail investor through over 200 branch offices in New York State."[16] This statement implies that Bankers Trust is selling, or intends to sell, commercial paper to the general public. And, we share your concern about the potential for widespread distribution of this paper. It also appears that the third requirement concerning "current transactions" may not be met because the promotional literature of Bankers Trust suggests that issuers use the proceeds from the sale of commercial paper to invest in other securities.[17]

This application of the definitions from the Securities Act to the terms of the Glass-Steagall Act would not only provide a consistent definition of "security" for these two contemporaneous Acts, but also would comport with the Congressional concerns behind the Glass-Steagall Act as described later in *Investment Company Institute* v. *Camp*, 401 U.S. 617 (1971). While your position paper contends that these concerns have little or no relevance to third-party commercial paper activities of banks, we believe that there is a significant connection between the commercial paper activities of Bankers Trust and the nine specific "hazards" that you enumerate in your posi-

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15 *See Sanders* v. *John Nuveen & Co., Inc.*, 463 F.2d 1075 (7th Cir. 1972), and *Franklin Savings Bank* v. *Levy*, [1975-76 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,389 (S.D.N.Y. 1975), where the courts found that commercial paper issued by corporations did not meet these four criteria.

16 Bankers Trust, *Commercial Paper Proposal: Bankers Trust Responds to Your Commercial Paper Needs* 3 (undated).

17 *Id.* at 5, 16. Securities Act Release No. 4412 specifically states that the "current transactions" requirement is not met if proceeds from the sale of commercial paper are used to purchase securities.

tion paper as underlying the passage of Sections 16 and 21 of the Glass-Steagall Act.

1. A commercial bank might invest its own assets in frozen or otherwise imprudent stock or security investments.

2. A commercial bank might be subject to new promotional and other pressures to shore up its securities affiliate through unsound loans or other aid.

The position paper appears to assume there is no possibility that imprudent investments might be made by a bank selling commercial paper. Instead, it seems to regard activities by banks in commercial paper as unquestionably prudent merely because they are inspected by bank examiners. However, Congress was very concerned that the promotional pressures and conflicts arising out of investment banking activities might detrimentally affect a bank's judgment regarding loans or investments in securities of particular issuers in which the bank also had a saleman's interest. *Camp,* 401 U.S. at 630-33. As pointed out by the Supreme Court, "[i]t was thought that the bank's saleman's interest might impair its ability to function as an impartial source of credit." *Id.* at 631 (footnote omitted), *citing* remarks of Senator Glass. Although banks originally conducted securities operations indirectly through securities affiliates, an interpretation permitting investment banking activities which potentially involve the same or similar abuses when conducted by banks directly would appear to permit form to triumph unjustly over substance. *Id.* at 629.

3. Public confidence in a commercial bank might be impaired should its affiliate perform poorly.

Commercial paper activities conducted directly by a bank, rather than indirectly through an affiliate, may in fact increase the risk that the public will lose confidence in the bank. As you point out, it may be true to some extent that public confidence in a commercial bank is "maintained through the examination process." However, to the best of our knowledge, bank exami-

nation procedures did not prevent the losses by even a single bank purchaser of Penn Central's commercial paper in 1970—despite the availability of public information which tended to indicate that the paper was of less than prime quality. *See, e.g., Penn Central Report, supra,* at 279, 289. To the best of our knowledge, there is also no examination procedure currently being employed to evaluate the soundness of commercial paper sold by a bank for an issuer. This is particularly important in light of the fact that purchasers of commercial paper from banks presumably rely at least as much as customers of broker-dealers upon the seller's prestige and reputation. *Id.* at 275. As the Supreme Court said: "Congress feared that the promotional needs of investment banking might lead commercial banks to lend their reputation for prudence and restraint to the enterprise of selling particular . . . securities, and that this could not be done without that reputation being undercut by the risks necessarily incident to the investment banking business." *Camp, supra,* 401 U.S. at 632 (footnote omitted).

4. A commercial bank might make its credit facilities more freely available or make unsound loans to those companies in whose stock or securities its affiliate has invested or become otherwise involved.

Congress recognized that the pressure to sell a particular investment might create a risk that a bank would make unsound loans to companies in whose securities an affiliate has invested or become otherwise involved. *Id.* at 631. It would seem equally true that a bank, under the same promotional pressure to sell a particular issuer's commercial paper because of its substantial involvement, would yield to its saleman's interest and make its credit facilities more freely available, or make unsound loans, to those issuers.

5. A commercial bank's saleman's interest might impair its ability to function as an impartial source of credit.

Congress indisputably prohibited commercial banks from engaging in activities such as underwriting securities, other

than government and municipal securities,—whether those securities be commercial paper or otherwise. *Id.* at 629. A prohibition against commercial banks engaging in such investment banking activities would not in any way interfere with their proper commercial banking functions; it ensures and enhances the ability of commercial banks to perform their credit allocation function impartially, removed from the inevitable conflicts present in the context of the promotional pressures of investment banking.

6. Commercial bank depositors might suffer losses on investments they had made in reliance on the relationship between the bank and its affiliates.

Despite your assertions, there is no real assurance that commercial paper has been sold by banks only to "sophisticated investors who are able to evaluate the benefits and risks associated with the purchase of commercial paper." Indeed, we note that the information provided prospective and actual purchasers may be inadequate to permit a full evaluation of the risks involved, and appears to fall short of the information broker-dealers may furnish commercial paper purchasers. *See Penn Central Report, supra,* at 290.

7. A commercial bank might undercut its reputation for prudence and restraint through the sale of stock and securities by assuming the risks "necessarily incident" to the investment banking business.

As you point out, the business of dealing in short-term credit may generally be less risky than the business of investment banking, but it is clearly not riskless. Especially in light of the Penn Central case, we cannot agree with your contention that market forces can be relied upon to "dictate that only the most credit-worthy corporations issue commercial paper." Moreover, since the same strict credit analysis applicable to a bank's own commercial paper investments may not be applicable where the bank sells such paper to its customers, it risks the loss of public confidence if such paper turns out to be an unsound invest-

ment. And, Congress sought to ensure that public confidence in commercial banks was in no way jeopardized by investment banking. *Camp, supra,* 401 U.S. at 634.

8. A commercial bank might make loans to customers in order to facilitate the purchase of stock and securities of a speculative nature.

Regardless of whether or not commercial paper investments may be categorized as "speculative"—a judgment which depends on the current financial soundness of each particular issuer—it is indisputable that such investments involve some risk, and at least to that extent a bank risks a loss of public confidence when customers purchasing from it incur losses. Moreover, a bank's promotional interest in selling commercial paper for an issuer may interfere with the impartiality expected of banks making loans. An obvious temptation exists for a bank to favor allocation of credit to customers purchasing paper in which the bank has a direct promotional interest. Furthermore, this promotional interest may compromise the obligation of commercial bankers to render disinterested investment advice. In this connection, the Supreme Court noted with approval the following statement from the Act's legislative history:

> Obviously, the banker who has nothing to sell to his depositors is much better qualified to advise disinterestedly and to regard diligently the safety of depositors than the banker who uses the list of depositors in his savings department to distribute circulars concerning the advantages of this, that, or the other investment on which the bank is to receive an originating profit or an underwriting profit or a distribution profit or a trading profit or any combination of such profits.

Id. at 633 (footnote omitted), *citing* 75 Cong. Rec. 9912 (remarks of Senator Bulkley).

Letter, dated April 20, 1979

9. An affiliate of a commercial bank might use the bank's trust department to unload excessive holdings of securities.

Although some conflicts might be removed if a bank were prohibited from placing commercial paper which it sells in trust accounts which it manages, similar conflicts nevertheless may exist with respect to correspondent banks, which may feel pressure to place such paper in trusts which they manage. Also, promotional conflicts may exist not only with respect to trust accounts, but also with respect to all those customers to whom the bank owes a fiduciary duty or who in any manner rely upon the bank to render disinterested advice. If these conflicts are reduced by preventing trust accounts or any other customers from purchasing commercial paper of particular issuers which the bank serves, this would allow banks to engage in investment banking at the expense of their customers who may be deprived of desirable investment opportunities.

These are, in sum, our three major concerns with your letter and position paper on the commercial paper activities of Bankers Trust. We shall be pleased to give you any further assistance you may desire in this matter.

Sincerely,

/s/ RALPH C. FERRARA
Ralph C. Ferrara
General Counsel

Letter, dated June 26, 1979, from Ralph C. Ferrara to Neal Petersen

[Letterhead of SECURITIES AND EXCHANGE COMMISSION]

June 26, 1979

Neal L. Peterson, Esq.
General Counsel
Board of Governors of the
Federal Reserve Sytem
Washington, D.C. 20551

Dear Neal:

This responds to your letter dated June 14, 1979, and the enclosure, the revised draft of a paper by the Board's Legal Division entitled "Commercial Paper Activities of Commercial Banks: A Legal Analysis." We appreciate this second opportunity to offer our comments with respect to the Board's position concerning the distribution of commercial paper by commercial banks. In view of your strict time schedule, and because we believe that many of the points we made in our letter of April 20, 1979, remain applicable, our comments in this letter will be limited. And, we emphasize that this letter has not been formally reviewed by the Commission. We reiterate, however, that we would appreciate an opportunity to present a more comprehensive analysis after Commission review, if your position paper comes before the Board of Governors.

The revised draft concludes that commercial banks may, incidental to, or as part of, the banking business: (1) sell commercial paper as agent for the issuer, provided that such sales are "limited to purchasers to whom commercial banks normally sell participations in loans;"[1] (2) purchase and sell commercial paper for their own account, again provided that

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1 The revised draft, in turn, refers to "institutional purchasers" as those to whom banks normally sell loan participations.

the sales are limited to institutional purchasers; and (3) buy commercial paper as agent for the account of any customer, and sell commercial paper as agent for the account of any customer who is not the issuer of the paper.

Assessing whether a bank's commercial paper activities are consistent with the requirements of the Glass-Steagall Act requires, in our view, a two-fold inquiry. First, Section 16 of the Glass-Steagall Act, 12 U.S.C. 24, ¶ 7, requires resolution of the question whether a bank's commercial paper activities constitute an exercise of "such incidental powers as *** [are] necessary to carry on the business of banking ***." But an affirmative answer to this first question is not dispositive of the lawfulness of those activities—a bank's commercial paper activities must also be found to fall outside those areas of securities activities which are specifically prohibited to banks under Sections 16 and 21 of the Glass-Steagall Act, 12 U.S.C. 24, ¶ 7 and 378.[2]

With respect to the latter inquiry, the revised draft employs the same mode of analysis and reasserts the same restrictive construction of the term "security" as did the initial draft. Accordingly, we continue to question the soundness of this approach. As we pointed out in our earlier comments, the staff's conclusion that the term "security," as used in Sections 16 and 21 of the Glass-Steagall Act, extends only to an "investment security" or a security that is "predominantly speculative in nature" appears at odds with both the language and legislative history of the Glass-Steagall Act.

The staff's revised position paper, like the earlier version, focuses on Congress' original use in 1933 of the term "invest-

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[2] Such an approach proceeds from the well-settled canon of statutory construction that specific terms prevail over the general. *See, e.g., Fourco Glass Co.* v. *Transmirra Products Corp.*, 353 U.S. 222, 228-29 (1957); *Clifford F. MacEvoy Co.* v. *United States*, 322 U.S. 102, 107 (1944); *Ginsberg & Sons* v. *Popkin*, 285 U.S. 204, 208 (1932); *Federal Trade Commission* v. *Manager, Retail Credit Co.*, 515 F.2d 908, 993-94 (D.C. Cir. 1975).

ment securities" in delimiting the scope of a bank's dealing and underwriting activities under Section 16 of the Glass-Steagall Act. But, as we noted in our earlier comments, two years after enactment of the Glass-Steagall Act, Congress amended Section 16 broadly to *prohibit* banks from dealing in or underwriting all "securities and stock"—not only "investment securities." By contrast, with respect to those securities which a bank is *permitted* to purchase for its own account, Congress in 1935 retained the narrower term "investment securities."

Moreover, neither the language of the original enactment of the Glass-Steagall Act in 1933, nor the amendments thereto in 1935, prohibit a bank from dealing in or underwriting only those securities which are "predominantly speculative in nature." And, we not persuaded, for the reasons we articulated in our earlier comments, that the legislative history of the Glass-Steagall Act supports assigning such a restrictive meaning to the term "securities and stock" under Section 16 of the Act. Similarly, the staff's reliance on the Board's letters to Congress during consideration of legislation which was to become the Securities Act of 1933 appears misplaced. While the Board urged Congress in that legislation to exclude commercial paper from the definition of a "security," Congress declined to adopt this approach. Rather, Congress, in Section 3(a)(3) of the Securities Act of 1933, exempted certain types of commercial paper from the registration requirements of the Act,[3] but defined a security under Section 2(1) to encompass commercial paper,[4] and extended the antifraud protections of the Act to

3 Section 3(a)(3) of the Securities Act, 15 U.S.C. 77c(a)(3), exempts from registration "any note *** which arises out of a current transaction or the proceeds of which have been or are to be used for current transactions, and which have a maturity at the time of issuance of not exceeding nine months."

4 Thus, Section 2(1) of the Securities Act, 15 U.S.C. 77b(1), defines a security, among other things, to include any "note" or "evidence of indebtedness."

Because Congress defined "security" to include commercial paper, we do not find persuasive the revised draft's reliance upon testimony

transactions in all securities, whether or not exempt from registration.[5]

As we suggested in our earlier comments, any interpretation of the term "securities" under the Glass-Steagall Act must be made in light of, and preferably consistent with, that term's definition under the Securities Act, since both pieces of legislation were considered concurrently by Congress and were enacted within weeks of each other.[6] Of course, as we noted in our earlier comments, definitions under Section 2 of the Securities Act apply "unless the context otherwise requires,"

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on the Securities Act given by Senator Glass in 1933, urging that banker's acceptances and commercial paper be exempted from the definition of security. *Hearings on S. 875 Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. 98 (1933). Indeed, if Senator Glass adhered to this view after passage of the Securities Act, it would seem logical that he would have attempted to incorporate into the Glass-Steagall Act a more restrictive definition of "security," so as to distinguish that term from the broader definition under the Securities Act.

5 *See* Securities Act of 1933, Sections 12(2) and 17(c), 15 U.S.C. 77*l*(2) and 77q(c).

6 In our earlier comments, we noted that the Board's staff, in construing the term "issue" for purposes of the Glass-Steagall Act, explained that "it is unlikely that Congress intended to give a content to the term as used in Glass-Steagall different from that given to the term in the Securities Act of 1933, which was enacted three weeks earlier." Federal Reserve Board Staff, *Commercial Bank Private Placement Activities* at 87 n.6 (1977). We noted further that the staff viewed the Securities Act's definition of "issue" to offer a "compelling analogy" to the meaning of that term under the Glass-Steagall Act. *Id.* at 89.

We do not perceive any basis for the distinction advanced in the staff's revised draft that definitions under the Securities Act which concern "securities activities, *e.g.*, 'issuing' and 'underwriting,' " may govern the meaning of terms used in both the Securities and Glass-Steagall Acts, but that the Securities Act definitions of "types of obligations" are not similarly applicable to the meaning of these terms under Glass-Steagall.

and, in light of this statutory proviso, courts have held that commercial paper arising from mercantile transactions is outside the definition of "security."[7] But, the mere fact that an instrument is called "commercial paper" is not determinative, since the application of the securities laws "turns on the economic realities underlying a transaction, and not on the name appended thereto." *United Housing Foundation, Inc.* v. *Forman*, 421 U.S. 837, 849 (1975). In applying this approach, courts have consistently found commercial paper to constitute "securities" under the federal securities laws where they entail an investment feature and do not merely evidence a mercantile transaction.[8]

The *in pari materia* approach which we suggest for defining "security" under the Glass-Steagall Act by reference to the Securities Act is not undermined, as the staff's revised position paper asserts, by judicial decisions which treat bank time deposits as securities under the securities laws. *See, e.g., Garner* v. *Pearson*, 374 F. Supp. 591, 596 (M.D. Fla. 1974). Construing time deposits to be "securities" issued by a bank

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7 *See Great Western Bank & Trust* v. *Kotz*, 582 F.2d 1252 (9th Cir. 1976). *Cf. C.N.S. Enterprises, Inc.* v. *G & G Enterprises, Inc.*, 508 F.2d 1354 (7th Cir.), *cert. denied*, 423 U.S. 825 (1975); *McClure* v. *First Nat'l Bank*, 497 F.2d 490 (5th Cir. 1974); *Lino* v. *City Investing Co.*, 487 F.2d 689 (3d Cir. 1973) (cases construing "security" under the Securities Exchange Act of 1934).

8 *See, e.g., Exchange National Bank of Chicago* v. *Touche Ross & Co.*, 544 F.2d 1126 (2d Cir. 1976); *Sanders* v. *John Nuveen & Co., Inc.*, 463 F.2d 1075 (7th Cir. 1972); *Franklin Savings Bank* v. *Levy*, [1975-76 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,389 (S.D.N.Y. 1975).

See also Securities Act Release No. 4412 (Sept. 20, 1961), where the Commission stated that commercial paper, in order to qualify for exemption from registration under the Securities Act, must be (1) prime quality paper, (2) not ordinarily purchased by the general public, (3) issued to facilitate well-recognized types of current operational business transactions, and (4) eligible for discounting at Federal Reserve banks.

under the Glass-Steagall Act has no disruptive effect on that statutory scheme. Sections 16 and 21 of the Glass-Steagall Act do not prohibit a bank from issuing its own securities, as opposed to dealing or underwriting the securities of others. Moreover, Sections 16 and 21 of the Glass-Steagall Act specifically refer to the receipt of deposits as a permissible activity of a commercial bank.[9]

As to the other inquiry under the Glass-Steagall Act—whether a questioned activity is incidental to the business of banking—the revised draft concludes that a bank's commercial paper activities, under certain limitations, would fall within the business of banking. However, we have serious reservations with respect to the specific approach adopted by the staff. Our reservations center on the adequacy of the restriction which the revised draft would impose upon sales of commercial paper by a bank as agent for an issuer and for its own account—namely, that such sales be limited to "institutional" purchasers to whom banks normally sell loan participations.

In the first place, as your revised draft acknowledges, loan participations themselves may constitute securities, subject to the antifraud provisions of the federal securities laws, particularly where multi-party, rather than two-party, loan participations are involved. Under such circumstances, the elements of a common enterprise and reliance by purchasers upon the enterpreneurial efforts of the lead bank may give rise to an investment contract. *See, e.g., Lehigh Valley Trust & Co.* v. *Central National Bank of Jacksonville,* 409 F.2d 989 (5th Cir. 1969). Accordingly, absent greater elaboration of current limi-

9 Thus, Section 16 of the Glass-Steagall Act provides that a national banking association shall have power to exercise "all such incidental powers as shall be necessary to carry on the business of banking; • • • by receiving deposits • • •;" and Section 21 prohibits any organization "engaged in the business of underwriting, selling or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes or other securities" from engaging at the same time "in the business of receiving deposits • • •."

tations on sales of the loan participations to which your revised draft refers, these participations themselves may raise questions under the Glass-Steagall Act.

Moreover, your draft does not define "institutional" purchaser or explain whether those institutions, in acquiring third party commercial paper, are under any constraints against selling that paper to general members of the public or other "non-institutional" purchasers. In this connection, we note that non-bank firms and individuals desiring to make short-term investments free of the interest rate restrictions which apply to traditional savings media are today major holders of commercial paper; these persons, absent appropriate restrictions, might well constitute the direct or ultimate purchasers of commercial paper handled by banks.[10] In addition, even assuming that limiting sales to current "institutional" purchasers could avoid Glass-Steagall problems, the revised draft contains no indication of whether banks could in the future sell commercial paper to non-institutional purchasers, if sales of loan participations are expanded to include such other purchasers.

As to a bank's purchase and sale of commercial paper for the account of its customers, the revised draft concludes that this activity is incidental to the business of commercial banking "[j]ust as section 16 of the Glass-Steagall Act authorizes national banks to purchase and sell securities and stock upon the order of and for the account of customers" [footnote omitted]. But the activities permissible under the Glass-Steagall Act on behalf of customers are circumscribed by the requirement that purchases and sales be "solely upon the order *** [of] customers." This language would appear to limit the discretion of banks in servicing the accounts of its customers and may also restrict certain forms of customer solicitations, such as advertising that promotes banks as "specialists" in the area of commercial paper.

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10 *See* R. Selden, *Trends and Cycles in the Commercial Paper Market* (1963); Note, *The Commercial Paper Market and the Securities Acts*, 39 U.Chi. L. Rev. 362, 369 (1972).

Letter, dated June 26, 1979

Finally, we reiterate our conclusion that a bank's dealings in, and underwriting of, commercial paper raises policy concerns, identified by the Supreme Court in *Investment Company Institute* v. *Camp*, 401 U.S. 617 (1971), that prompted Congress to pass the Glass-Steagall Act. As discussed more fully in our earlier letter, Congress, in passing the Glass-Steagall Act, sought to insulate commercial banks from the "subtle hazards" that inevitably result when banks engage in securities dealings. These hazards, in our view, may be present where a bank distributes third party commercial paper among an undefined and unlimited number of "institutional" purchasers. Thus, a bank that distributes third party commercial paper, like a bank that underwrites an issue of equity stock, may jeopardize its reputation for prudence and restraint in promoting those securities, regardless of whether they may be characterized as more or less "conservative" investments. *Id.* at 637. Further, the salesman's interest which a bank has in a company's commercial paper might distort its credit decisions or lead the bank to make unsound loans either to the company, *id.* at 631, or to those who would use the proceeds to finance the purchase of securities promoted by the bank. *Id.* at 632. In short, we continue to question whether the promotional stake of a bank engaged in the underwriting, distribution, and sale of commercial paper will not be "destructive of prudent and disinterested commercial banking and of public confidence in the commercial banking system,"—evils which Congress sought to eliminate through passage of the Glass-Steagall Act. *Id.* at 634.

The foregoing summarizes our concerns with the revised staff position paper. Of course, we shall be pleased to provide any further comments which you may desire in this matter.

Sincerely,

/s/ RALPH C. FERRARA
Ralph C. Ferrara
General Counsel

Letter, dated June 28, 1979, From Neal L. Petersen, to James J. Baechle

[Letterhead of Board of Governors of the Federal Reserve System]

June 23, 1979

Mr. James J. Baechle
Senior Vice President and
General Counsel
Bankers Trust Company
280 Park Avenue
New York, New York 10015

Dear Mr. Baechle:

I am writing with regard to certain activities of Bankers Trust Company in the purchase and sale of third-party commercial paper. From your letters dated December 22, 1978, with enclosures, and February 1979, it is understood that Bankers Trust acts as agent for issuers in the sale of commercial paper, and, in connection with such activity, provides financial advisory services to issuers of commercial paper, provides extensions of credit at or near the commercial paper rate to issuers of commercial paper, and purchases and sells commercial paper in the secondary market. I have concluded that it is incidental to the business of commercial banking for a commercial bank to purchase commercial paper for the account of any customer and to sell commercial paper for the account of a customer who is not the issuer of the paper as agent of the customer, and that it is the business of commercial banking for a commercial bank to sell commercial paper as agent of the issuer of the paper and to purchase and sell commercial paper for the bank's own account, provided that the sales as agent of the issuer of the paper and for the bank's own account are limited to purchasers to whom commercial banks normally sell participations in loans. I have further concluded that such activities are not prohibited by the Glass-

Steagall Act. The bases for these conclusions are discussed in "Commercial Paper Activities of Commercial Banks: A Legal Analysis," a copy of which is enclosed.

In the February 2, 1979, letter, you state that all commercial paper for which Bankers Trust acts as agent of and financial advisor to the issuer is exempt from the registration requirements of the Securities Act of 1933 by section 3(a)(3) of that act. Section 3(a)(3) of the Securities Act of 1933 as interpreted by the Securities and Exchange Commission and the courts exempts from the registration and prospectus requirements of that act only prime quality, negotiable paper that is issued to facilitate well-recognized types of current operational business requirements, is of a type that is not ordinarily advertised for sale to and purchased by the general public, has a maturity at the time of issuance of not exceeding nine months, and is of the type eligible for discount at a Federal Reserve Bank. In the promotional literature regarding the commercial paper activities of Bankers Trust, the class of potential purchasers of the commercial paper that Bankers Trust distributes is described as including a very large, diverse group of over 3,000 institutional purchasers in a variety of economic sectors and geographical regions, as well as retail purchasers. To constitute commercial paper, the paper must be sold to sophisticated purchasers and not to members of the general public. Further, to constitute the business of commercial banking, sales of commercial paper by a commercial bank as agent of the issuer of the paper and for the bank's own account should be limited to purchasers to whom commercial banks normally sell participations in loans. Accordingly, Bankers Trust must conform its commercial paper activities to this limitation.

In the December 22, 1978, letter, you state that Bankers Trust does not place the commercial paper of an issuer in accounts managed or advised by the trust department of Bankers Trust. Such practice is necessary to avoid possible conflicts of interest and should continue.

Letter, dated June 28, 1979

You state in the December 22 letter that Bankers Trust acts as agent for its parent bank holding company in the solicitation of orders for and in the sale of commercial paper issued by the holding company. The question whether such activity is an appropriate banking practice is not an issue addressed in the enclosed legal analysis of commercial paper activities of commercial banks.

If you have any questions regarding the conclusions of this letter or the enclosed legal analysis, you may contact me (202-452-3293) or Mr. John Walker (202-452-2418) of my staff.

Very truly yours,

/s/ NEAL L. PETERSEN
Neal L. Petersen
General Counsel

Enclosure

Excerpt from "Commercial Paper Activities of Commercial Banks, A Legal Analysis," Legal Division, Board of Governors of the Federal Reserve System

COMMERCIAL PAPER ACTIVITIES OF COMMERCIAL BANKS: A LEGAL ANALYSIS

Legal Division

Board of Governors of the Federal Reserve System

June 28, 1979

[material deleted]

of any customer and to sell commercial paper for the account of a customer who is not the issuer of the paper as agent of the customer, and it is the business of commercial banking for a commercial bank to sell commercial paper as agent of the issuer of the paper and to purchase and sell commercial paper for the bank's own account, provided that the sales as agent of the issuer of the paper and for the bank's own account are limited to purchasers to whom commercial banks normally sell participations in loans. Such activities do not violate sections 16 and 21 of the Glass-Steagall Act and are appropriate activities for commercial banks.

Letter dated February 20, 1980, from Ralph C. Ferrara to Theodore E. Allison

[Letterhead of Securities and Exchange Commission]

Theodore E. Allison
Secretary
Board of Governers of the
Federal Reserve System
20th & C Streets, N.W.
Washington, D.C. 20551

Dear Mr. Allison:

This Office has been advised that the Board of Governors of the Federal Reserve System (the "Board") will review the conclusion of the Board's General Counsel that the sale of third party commercial paper by Bankers Trust Company, if restricted to purchasers to whom commercial banks normally sell loan participations, is incidental to the business of banking and does not violate the Glass-Steagall Act.

As you may be aware, Neal L. Petersen, General Counsel to the Board of Governors, sent this Office, under covering letters dated April 12, 1979 and June 14, 1979, copies of (1) draft letters to Bankers Trust Company and (2) draft position papers of the Board's Legal Division entitled "Commercial Paper Activities of Commercial Banks: A Legal Analysis," and requested comments on these documents. In response to these requests, this Office submitted comment letters dated April 20, 1979 (Exhibit A), and June 26, 1979 (Exhibit B). We emphasized in each submission that the Commission had not formally reviewed this matter, and requested an opportunity to present additional comments, after formal Commission review, if the Board of Governors determined to review the staff's action.

The Commission has authorized me to inform you that it has reviewed, and concurs with, the letters of this Office dated April 20, 1979 and June 26, 1979. The Commission respect-

Letter, dated February 20, 1980

fully requests that these letters be presented to the Board of Governors for their consideration.

Sincerely,

/s/ RALPH C. FERRARA
Ralph C. Ferrara
General Counsel

Memorandum, dated May 8, 1980, to Files from Mr. Ashton and Ms. Fein Re: Meeting with Bankers Trust Officials

May 8, 1980

Files — Meeting with Bankers Trust

Mr. Ashton and Ms. Fein — officials.

On March 20, 1980, we met in New York with officials of Bankers Trust Company (Mr. James Baechle, General Counsel, and Mr. Garrett Thunen, Senior Vice President) to discuss Bankers Trust's commercial paper sales activities. Also present at the meeting were Robert O'Sullivan, Lawrence D. Fruchtman, and Al Toss of the New York Reserve Bank, and John Barnum and Jennifer Sullivan of the firm of White and Case, counsel to Bankers Trust. The purpose of our visit was to update information submitted by Bankers Trust on its commercial paper activities and to observe their commercial paper operations in preparation for Board review of petitions by A. G. Becker, Inc. and the Securities Industry Association challenging such activities. The following findings are based on our conversation with the Bankers Trust officials, and will be confirmed to the extent possible by Reserve Bank examiners during a general examination of the Bank commencing on April 1st:

I. *Organization*

[Material deleted]

II. *Description of Transactions*

1. Bankers Trust has sold commercial paper for issuers, with an average of about at present.
2. of the issues are split with another dealer.
3. The average note sold by Bankers Trust is approximately $1 million. The minimum denomination Bankers Trust will sell is $100,000. Maturities of notes sold average 60 days.

Memorandum, dated May 8, 1980

III. *Issuers*

[Material deleted]

IV. *Sales Activities*

[Material deleted]

V. *Purchasers*

[Material deleted]

2. Bankers Trust does not sell commercial paper to its trust department's discretionary accounts. If a Bankers Trust trust customer wishes to purchase commercial paper that Bankers Trust is selling as agent, however, the sale is made through the trust department.

3. Bankers Trust sells commercial paper mainly to corporations, other banks, including correspondent banks for their own account, and trust and pension funds. Bankers Trust does not sell to individuals. Purchasers also buy other short term investments sold by Bankers Trust.

4. The number of purchasers for each issue averages about 5 and usually no more than 15.

5. As far as Bankers Trust was aware, all purchasers were final investors. No resale of paper was contemplated.

6. Purchasers are usually, but not always, Bankers Trust customers.

7. There is no evidence that purchasers used borrowed funds to buy the commercial paper.

VI. *Conflicts of Interest*

[Material deleted]

cc: Messrs. Petersen, Mannion, Schwartz & Plotkin

Transcript of Board Deliberations on August 22, 1980 concerning SIA Petition [R. 647-658]

BOARD MEETING—FRIDAY, AUGUST 22, 1980
Agenda Item #4

Discussion regarding consideration of the petitions for review of activities for a State member bank with respect to commercial paper.

VOLCKER: Well, let me just say we are recording this discussion of this enforcement action brought with respect to Bankers Trust, and we do think that the meeting is properly closable, but a good deal of the discussion may be usually available for publication within a short period of time so long as those elements that are of concern with respect to a closed meeting could be deleted, and we're proceeding on that basis. I think on that understanding, why don't you proceed, Mr. Counselor.

PETERSEN: Thank you, Mr. Chairman. Mr Ashton of my staff will give the presentation on this matter.

ASHTON: Mr. Chairman, when this matter was last considered by the Board, some members of the Board expressed concern that commercial bank involvement in the sale of third party commercial paper may, at least in some circumstances, give rise to unsafe practices or potential conflicts of interests. Subsequently, at the request of Governor Partee, the Examination Council apponted a task force to consider the drawing up of guidelines that would govern in general the sale of third party commercial paper by banks. The task force has met and is presently considering drawing up such guidelines. The task force has met and is presently considering drawing up such guidelines. In view of the fact that the petitions by the Securities Industry Association and by A. G. Becker have been pending for a substantial period of time. And in view of the fact that the implementation of any guidelines drawn up at the Exam Council would necessarily involve some further delay, we believe that it's advisable at this time to act on the SIA and

A. G. Becker petitions without further delay. As explained in a previous memorandum, we believe [material deleted]

PETERSEN: When we say expand, we mean not change the nature of the activity beyond what they are presently doing, but we don't mean they have to confine their customers, for example, to what they are already doing.

SCHULTZ: When you say no other State member bank, you also mean bank holding companies as well?

ASHTON: I assume that that probably would apply, but we're not aware of any bank holding companies that are even interested in this. The only interest we've heard is from banks. They're doing it through their dealer departments.

PLOTKIN: That would be a new activity, Governor Schultz, which is not on the permitted list.

PARTEE: The difficulty here is we don't have the authority to specify this for national banks. We don't have the authority to specify what the restraint should be on the activity on the part of national banks. That's why I wanted to refer the matter to the Examinations Council.

VOLCKER: But if a bank can do it, can't a holding company do it? The argument here is that this is a banking function. Can't a holding company . . . . .

PETERSEN: They would have to apply to do it as a new activity.

VOLCKER: But would we have any banks . . . . . I guess I don't understand that. Are we in the business of prohibiting a holding company from doing something that the bank itself can do?

PETERSEN: No, we're not in that business.

VOLCKER: Do we ever do it? Do we have any grounds for doing it?

Transcript, August 22, 1980

PETERSEN: Well, yes, I suppose holding companies don't accept deposits and issue checking accounts and things like that so there could be some distinction if a holding company chose to enter into this activity, they would either have to file an application under section 4(c)(8) or possibly make the argument it would be permitted under 4(c)(5), which is a statutory provision that says, basically, that if a national bank is specifically or a bank is specifically authorized to do something the holding company would be able to . . . .

VOLCKER: Well, that's what I had in mind. Why wouldn't they argue that?

PETERSEN: It's possible they would.

VOLCKER: I think offhand I would find it very difficult to say that a holding company couldn't do this if a bank could do this.

PARTEE: Well, if a holding company were to come to us I'm inclined to think that you're correct that we would determine that since this must be closely related to banking because this is what banks do.

VOLCKER: Which is the whole issue to this legal argument.

PARTEE: That's right. But no one has come to us.

ASHTON: And we don't have any indication that they will in the near future.

PARTEE: But in the meantime . . . .

VOLCKER: They actually have to come to us even if they argue this other provision applies?

PETERSEN: It would be the better part of valor. Technically, you don't need an application, I believe, under section 4(c)(5).

MANNION: 4(c)(5) only allows you to acquire shares, doesn't allow you to engage in the activity.

VOLCKER: How much interest do we have among other banks in this matter?

Transcript, August 22, 1980

PETERSEN: Well, as far as any direct contact with the Board on this matter, I am not aware of any specific request. I understand but I can't say with certainty that there are some national banks that are interested in this activity.

ASHTON: Well, Bankers Trust told us that they had heard in the street that Citibank was thinking of doing it and I think staff may have gotten a couple of phone calls—one from Mellon in Pittsburgh and there may have been a couple of others—just inquiring generally about the status of the Bankers Trust matter.

PARTEE: I think it might develop with a few big banks, Paul, as an extension of the service of money management.

VOLCKER: Well, I'm a little surprised it hasn't developed. This is why I asked the question—why hasn't it developed?

PETERSEN: I think a number of institutions may be waiting for the final resolution of this particular proceeding before committing any resources to this activity with the possible exception of Citibank and maybe a couple of others.

VOLCKER: Well, the way this thing has been structured, we got a legal question and we've got a policy question. I take it you think there's a high probability that whatever way our decision goes, it will be contested.

PETERSEN: From all indications, Mr. Chairman, I would expect that it would be challenged.

VOLCKER: Well, I have a few questions about the implication and strategy involved assuming that the thing is going to be challenged.

[material deleted]

However, I have not seen the SEC brief and briefs tend to be persuasive when you read one side of it and then the other side tends to be persuasive too. What do they say on that point?

Transcript, August 22, 1980

PETERSEN: Well, Mr. Ashton, I want to comment that the SEC's arguments were reflected in the original memorandum to the Board.

ASHTON: Their argument is based on a definition in the Securities Act. The Securities Act of 1933 defines "security" to include all notes but then exempts commercial paper.

(VOLCKER OUT BRIEFLY.)

ALLISON: Could we wait a minute. Does any other Board Member have something to ask in the meantime?

PARTEE: Well, I did want to ask about the legal argument—about the question of the propriety of the activity so far as it's now engaged in by Bankers. As I understand it, first of all the accusations. They don't take these notes into account and then sell them out but they sell them on behalf of the corporation?

ASHTON: That's what they say but there are two modifying conditions. First of all, they told us that the parent holding company does purchase paper that the bank is selling for the holding companies own account. Now we haven't been able to connect that up to show that it's like an underwriting. The holding company may be holding it as a permanent investment but they said it's possible that the holding company may have sold the paper out of the holding company's portfolio which makes it look sort of like an underwriting. The other thing that qualifies it is Bankers Trust will make a loan at the commercial paper rate for a portion of the unsold proceeds of the paper that the bank is trying to sell.

PARTEE: Well, that is they undertake to sell the paper on the best efforts basis to the extent that it isn't sold within whatever time frame that is agreed to why they will fund the corporation with a loan.

ASHTON: With a loan at the commercial paper rate and I think it's at the end of the selling day.

PARTEE: At the end of the selling period.

PLOTKIN: They make no commitment to the issue that they will sell. They state that if there is any unsold amount, they will then advise the issuer and the issuer will ask whether they will purchase the unsold amount. It is done by the same group—operating people—in the bank. They say they take the paper back—if they make a loan, they take the paper back as collateral and then may sell it out as the market permits in the next few days and you do have the question though that they can still purchase the same paper for their own investment account and then when it gets into the question that we did find out that they purchased some of the paper in the holding company they did state that it was their policy that they would apply the bank's legal lending limit to any purchase of paper whether in the investment portfolio of the bank or in the bank holding company.

PARTEE: Well, you say they purchase it for their investment account but in fact, they purchase it as a loan and then shows in commercial loans for the enterprise and that's particularly with blind statements. But the total—the lending limit in their view would apply to what—to their total holding or to the total of the issue?

PLOTKIN: To their total holding but not to the total of the issue.

PARTEE: And they have no responsibility, implied or otherwise, to have to buy back these notes from the market.

PLOTKIN: That is their view.

PARTEE: And that's stated? Is it stated?

PLOTKIN: I think that was stated to us.

PARTEE: Well, I mean is it stated in the papers and stuff? Was it understood by investors and by the issuing corporation?

Transcript, August 22, 1980

PLOTKIN: In the investment—commercial paper being short-term obligations—there is a secondary market but a very small secondary market for commercial paper. I think you have in your memo, Rich, that they did state to us that if somebody did want a purchaser of commercial paper—did want to resell to them—they would then consider it at that time.

ASHTON: That's right, as an accommodation to the purchaser.

VOLCKER: I thought I saw some place in here that they did occasionally do that.

PLOTKIN: They did occasionally do that.

ASHTON: Apparently that's common practice in the commercial paper business.

VOLCKER: Who is on their customer list?

PARTEE: I was going to ask that too.

ASHTON: They supplied us with the names of 9 companies for which they had . . .

VOLCKER: For which they issue. I saw that but . . .

ASHTON: To whom do they sell?

VOLCKER: Who do they sell to?

PLOTKIN: They're customers who generally deal in short-term obligations. It's their short-term, it's the money market desk . . . .

[material deleted]

VOLCKER: I am not clear at this point on the non-legal aspect, just the policy aspect of this. What kind of a recommendation do we have from Supervision and Regulation?

RYAN: Well, Mr. Chairman,

[material deleted]

Transcript, August 22, 1980

SCHULTZ: That's where we seem to keep coming back to. The simple reason that it gets hard as hell to find any reason to turn it down on a legal basis.

PARTEE: Well, I think the legal case is pretty persuasive and that it is not a security.

SCHULTZ: I think it is too and given that it's difficult to find any good sound reason for turning it down but you do have these nagging worries and so you say let's button it up as best we can to protect against possible dangers in the future.

GRAMLEY: Well, the Legal Division did make that point that is regard to public policy issue at the moment. There's no reason for thinking that there's anything that's adverse to public interest in what's going on now. That does not seem to impose any significant problems. Isn't that correct?

PETERSEN: With respect to Bankers Trust?

GRAMLEY: Yeah. I don't think that basis is open to us for denial at this point. It seems to me that on both grounds—both legal grounds and policy grounds—the only option to us is to go ahead and permit the bank to engage in this activity and then cover ourselves with a set of specifications as what constitutes appropriate behavior in this market.

VOLCKER: I can't say as I don't think we don't have an option because there are lots of things where you could say I don't see any present abuse but I'm worried enough about the future so I'm going prohibit—

[material deleted]

PETERSEN: That would be something for everybody.

VOLCKER: I'm not suggesting we propose a change of law at this point unless we feel more strongly than we probably do. But . . .

PARTEE: I don't see any basis for it right now, Paul, but it might prove to be necessary.

VOLCKER: But then we've got some concerns about the desirability of this from our safety and soundness standpoint as it might be expanded. We may not have any concerns about Bankers Trust in the long run, I think that we don't. Therefore, we want to write in effect the regulation or a guideline—I'm not sure we're in a position to be fully satisfied about that guideline at the moment and therefore make a decision. We can make a decision to the extent of saying that's the direction we want to go but do we need something before us in the way of a guideline before we say this . . . .

PETERSEN: Mr. Chairman, bear in mind that this particular decision you have to make here today is whether or not we issue a cease and desist order against Bankers Trust to cause them to stop in their tracks so I think the approach of saying no, you don't have to stop in your tracks but don't change the nature of your activity and be on notice that you and other institutions may be subject to some further guidelines and restrictions on this activity in the future would be the proper way to go.

VOLCKER: I don't think that we want to say, I don't think that everything they're doing now is fine. That may be the case but I'm not sure we want to commit ourselves to that right at the moment.

PETERSEN: Well, we wouldn't . . . .

VOLCKER: I mean these questions of

PARTEE: Well, it'll take a little while, Paul, to get a proposed guideline back to the Board because of course the Board has no authority to impose any guidelines on national banks and therefore it's got to work through the Examination Council route in order to be effective.

VOLCKER: Well, what we're saying and this may not be any different from what you say but I think it's slightly different in tone from this thing I saw that on the issue presented to us of

the legal—cease and desist—in effect on the legal grounds that they're violating the Glass-Steagall Act we reject. We are more broadly examining the issue from the safety and soundness standpoint and we're not asking Bankers Trust to do anything at the moment but we are engaged with other agencies and intend to develop some guidelines which may or may not permit them to do what they're now doing. They don't have to change anything now but we are looking at it from that standpoint and in cooperation with the other agencies.

PETERSEN: That's basically what I had in mind.

VOLCKER: I got the tone from what you had written that everything they're doing now is okay.

PARTEE: And I think that's a good point to make, that we don't necessarily approve every jot and tittle in this operation.

VOLCKER: In fact it's approved on an interim basis because we're not doing anything about it. We're kind of warning them that we're going to come up with some guidelines that may in a fact affect the way they've been doing things.

PARTEE: And that can be reflected in the letter without much trouble.

VOLCKER: And I think you've got some suggestions as how to proceed on the guidelines and you come back to us on that issue when you're ready. I guess we probably need a formal vote on this one. I don't know whether the question has been defined clearly enough. I think the specific question is no cease and desist on the grounds of the Glass-Steagall Act and we're taking no other action at the moment. The rest of it is in the nature of more informal guidance and expression of our intention to look at this thing carefully from the safety and soundness standpoint as part of the bank regulatory function rather than as part of Glass-Steagall.

PETERSEN: Mr. Chairman, perhaps Mr. Ashton can expand on a couple of other technical issues that are before the Board in terms of the formal hearing request as I recall.

ASHTON: The request by counsel for A.G. Becker for oral argument, not a hearing, oral argument before the Board which was just reiterated recently and we have recommended that that request be denied since the issue was essentially a legal one that has been covered adequately in the voluminous pleadings that have been submitted over the last 18 months and we don't believe that oral argument before the Board would serve any purpose and we're recommending that that additional request be denied at the same time the petition for cease and desist order are also denied.

VOLCKER: I assume that we are following that.

PARTEE: It seems to me that we are thoroughly steeped at this point with issues we've had.

VOLCKER: I think that we'll have a vote on this.

ALLISON: Vice Chairman Schultz?

SCHULTZ: Yes

ALLISON: Governor Partee?

PARTEE: Yes or no?

SCHULTZ: The recommendation asserts that we not issue a cease and desist order and I'm favoring the recommendation.

VOLCKER: And that we not have an oral hearing.

PARTEE: I agree.

GRAMLEY: I agree.

VOLCKER: Yes.

Letter of the Board, dated September 26, 1980, in response to petitions concerning sale of third party commercial paper by Bankers Trust Co.

[Letterhead of Board of Governors of the Federal Reserve System]

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Gentlemen:

This is in reference to petitions submitted to the Board by the Securities Industry Association (the "SIA") and A.G. Becker, Incorporated ("A.G. Becker") requesting that the Board prohibit Bankers Trust Company, New York, New York ("Bankers Trust"), a State member bank, from selling commercial paper issued by companies not related to the bank ("third party commercial paper"). The SIA and A.G. Becker allege, among other things, that Bankers Trust's sale of third party commercial paper violates the Glass-Steagall Act and must be prohibited by the Board.

In July 1978, Bankers Trust was reported to have placed several issues of third party commercial paper on behalf of certain corporate issuers. Shortly thereafter, the SIA, a national trade association of securities brokers, dealers, and underwriters, and A.G. Becker, one of the recognized dealers in commercial paper, requested Board staff to review the legality of such activities. On June 28, 1979, after the submission of written comments by interested parties, including the General Counsel of the Securities and Exchange Commission

Letter, dated September 26, 1980

("SEC"), the Board's Legal Division issued a legal analysis dealing in general with commercial paper activities by commercial banks. The analysis found that it is the business of commercial banking for a commercial bank to sell third party commercial paper as agent of the issuer or for the bank's own account, provided that such sales are limited to institutional purchasers to whom commercial banks might in the normal course of business sell participations in loans. The opinion also concluded that such activities did not violate the Glass-Steagall Act. By letters dated June 29, 1979, the General Counsel advised the SIA and A.G. Becker that the Board had not considered the matter but that the Legal Division would recommend that the Board do so if those organizations requested.

On July 26, 1979, the SIA submitted to the Board a petition requesting that the Board formally review the matter and order Bankers Trust to cease and desist from all its third party commercial paper activities. By letter dated January 31, 1980, A.G. Becker made clear that it wished its previous submissions presented to the Board. In addition, by letter dated February 20, 1980, the General Counsel of the SEC stated that the Commission had reviewed and concurred with the views expressed by the SEC's General Counsel in his comments to the Board's General Counsel on these issues.

In requesting that the Board review the selling of commercial paper by Bankers Trust, the SIA and A.G. Becker claim that Bankers Trust is engaged in underwriting or dealing in a security in violation of the Glass-Steagall Act and that such activities will result in the kinds of risks to the bank and potential conflicts of interest that the Act was intended to eliminate. In addition, A.G. Becker claims that the selling of third party commercial paper by commercial banks will have other adverse effects that warrant prohibition of the activities on public policy grounds. The comments of the SEC generally agree with the Glass-Steagall Act arguments of the SIA and A.G. Becker.

Letter, dated September 26, 1980

In acting on the petitions of the SIA and A.G. Becker, the Board has considered the legal analysis of the Board's Legal Division concerning commercial paper activities of commercial banks as well as the submissions of all the interested organizations, including those of the SIA, A.G. Becker, Bankers Trust, and the SEC, and information on Bankers Trust's commercial paper activities obtained from officials of the bank.

The Board has determined to deny the petitions of the SIA and A.G. Becker to the extent such petitions allege that Bankers Trust's commercial paper activities violate the Glass-Steagall Act or that such activities should be prohibited by general considerations of public policy.

The Board has concluded that, with respect to the alleged violation of the Glass-Steagall Act, the stronger argument is that the financing instrument commonly referred to as commercial paper is not a "security" within the meaning of the Glass-Steagall Act. The restrictions of the Act against underwriting and dealing in securities thus do not apply to such an instrument. The Board has also determined that the general considerations of public policy advanced by A.G. Becker, such as allegedly unfair competitive advantages by banks in selling commercial paper, do not at this time warrant prohibition of Bankers Trust's commercial paper activities.

In the Board's view, however, the sale of third party commercial paper by a commercial bank could involve, at least in some circumstances, potential unsafe or unsound banking practices. Accordingly, the Board, in cooperation with the other bank regulatory agencies, has initiated the process of developing guidelines designed to prohibit potential unsafe or unsound practices in the sale by a bank of third party commercial paper. The Board, therefore, is taking no action regarding petitioner's contentions of dangers to Bankers Trust and potential conflicts of interest and will consider these issues in the context of the Board's consideration of such general guidelines.

Letter, dated September 26, 1980

Finally, the Board finds that the issues involved in these petitions are primarily legal in nature and have been adequately addressed in the many written submissions of the petitioners, the SEC, and Bankers Trust. Accordingly, the request by A.G. Becker for oral argument before the Board on this matter is denied.

The reasons for the Board's actions are set forth in detail in the accompanying Statement Regarding Petitions To Initiate Enforcement Action.

Very truly yours,

(signed) THEODORE E. ALLISON
Theodore E. Allison
Secretary of the Board

cc: William C. Knox, Jr., Esq.
John W. Barnum, Esq.
James J. Baechle, Esq.
Ralph C. Ferrara, Esq.

Federal Reserve System, *Statement Regarding Petitions to Initiate Enforcement Action*, dated September 26, 1980

STATEMENT REGARDING PETITIONS
TO INITIATE ENFORCEMENT ACTION

The Securities Industry Association (the "SIA") and A.G. Becker, Incorporated ("A.G. Becker") have requested the Board to prohibit Bankers Trust Company, New York, New York ("Bankers Trust"), a State member bank, from selling commercial paper issued by companies not related to the bank ("third party commercial paper"). The SIA and A.G. Becker allege that Bankers Trust's sale of third party commercial paper violates the Glass-Steagall Act, which generally prohibits banks from underwriting or dealing in securities. A.G. Becker also contends that considerations of public policy militate against permitting Bankers Trust from selling third party commercial paper.

Bankers Trusts' Sales Activities

Commercial paper refers to prime quality, negotiable, usually unsecured short-term promissory notes issued by business organizations to meet part of their short-term credit needs.[1] Commercial paper is offered and sold to sophisticated purchasers, rather than to the general public, through dealers or directly by the issuer. Because commercial paper is usually unsecured, issuers are generally large, well-known, and financially strong businesses. Most commercial paper has an initial maturity of 60 days or less and the paper sold by dealers is issued in denominations usually ranging from $100,000 to $1 million or more. Purchasers of commercial paper are mostly large institutions with idle short-term funds to invest. Commercial paper is considered relatively risk-free; interest rates on

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1 For a more detailed description of the commercial paper market *see* Hurley, The Commercial Paper Market, 63 Fed. Res. Bull. 525 (1977) [hereinafter cited as "Hurley"] and Comment, *The Commercial Paper Market and the Securities Acts*, 39 U. Chi. L. Rev. 362 (1972).

commercial paper are usually slightly above the rates on short-term United States government obligations, such as Treasury bills. The proceeds of commercial paper traditionally have been used for current or seasonal needs.

Bankers Trust represents that it is selling third party commercial paper only as the agent of the issuer and that the bank is not, like the commercial paper dealers, acting as a principal in such sales. Bankers Trust does not purchase, or make any commitment to purchase, the commercial paper the bank sells as agent. On some occasions, however, Bankers Trust extends credit (without any prior commitment), at or near the commercial paper rate, to issuers of paper sold by the bank in an amount representing a small portion of the unsold amount of the issue. The notes representing such loans may subsequently be sold. The bank's parent holding company has purchased for its own account commercial paper sold by the bank.[2]

Bankers Trust states that it does not tie the use of its other services to its commercial paper selling services and does not offer special inducements to issuers using such services. Bankers Trust sells only prime quality commercial paper of issuers that have the highest rating from at least one of the rating services that rate commercial paper issuers.

The customers to whom Bankers Trust sells commercial paper are usually part of Bankers Trust's established base of institutional investors that regularly purchase from the bank other short-term instruments in which the bank deals. Bankers Trust does not sell to individuals or to its trust department accounts.

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2 The bank also provides financial advice to issuers with regard to the issuance of commercial paper and serves as settlement agent for purchases of commercial paper. None of these activities has been directly challenged. Bankers Trust also sells as agent commercial paper issued by its own parent holding company. The Legal Division's analysis expressed no opinion on this activity and it is not involved in the present petitions.

Statement Regarding Petitions to Initiate Enforcement Action

The Glass-Steagall Act Issues

The Banking Act of 1933 contains four provisions (collectively referred to as the Glass-Steagall Act) that restrict participation by banks and affiliates of banks in specified securities activities. The provisions involved here are sections 16 and 21 of the Act, the provisions that apply to banks.[3] Section 16 provides in relevant part:

> The business of dealing in securities and stock by the [national bank] shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of customers, and in no case for its own account, and the association shall not underwrite any issue of securities or stock. 12 U.S.C. § 24 Seventh.

Section 5(c) of the Glass-Steagall Act, 12 U.S.C. § 335, provides that State member banks are subject to the limitations of section 16 with respect to dealing in securities.

Section 16 carves out an exception to the general prohibition against involvement with securities by providing that national banks (and consequently State member banks) may purchase for their own account "investment securities" as defined in the statute.[4] "Investment securities" are defined by section 16 generally as marketable debt obligations commonly known as investment securities under such further definition prescribed by the Comptroller of the Currency. The Comptroller's regula-

3 Section 20 of the Act, 12 U.S.C. § 377, prohibits affiliates of banks from "engaging principally in the issue, flotation, underwriting, public sale or distribution" of securities. In addition, section 32 of the Act prohibits member banks from having director, officer, or employee interlocks with companies "primarily engaged" in the securities business.

4 Section 16 makes a further distinction with respect to investment securities. Banks may *underwrite* and *deal in* (as well as purchase for their own account) certain kinds of investment securities: obligations of the United States, general obligations of states or political subdivisions of states, and obligations of or guaranteed by certain government agencies.

tion, 12 C.F.R. § 1.3(b), defines "investment security" as a marketable debt obligation "commonly regarded as an investment security" and not "predominantly speculative in nature."

Section 21 of the Glass-Steagall Act provides that it is unlawful

> For any person, or . . . organization, engaged in the business of issuing, underwriting, selling, or distributing, . . . stocks, bonds, debentures, notes, or other securities, to engage at the same time . . . in the business of receiving deposits. 12 U.S.C. § 378(a)(1).

Section 21 further provides that its restrictions do not prohibit any bank from "dealing in, underwriting, purchasing, and selling investment securities, or issuing securities" to the extent such activities are permissible under section 16.

Thus, both section 16 and section 21 recognize a distinction between "investment securities" and other kinds of securities. Banks in general may invest in, *but not* underwrite or deal in (with limited exceptions), investment securities; banks are barred from issuing, purchasing for their own account, underwriting, or dealing in securities that do not qualify as investment securities.[5]

The contentions of the SIA and A.G. Becker that Bankers Trust is violating these statutory prescriptions are based on the contentions that (1) commercial paper is a "security" for purposes of the Glass-Steagall Act and (2) Bankers Trust's selling activities constitute the forbidden underwriting and dealing in securities. Additionally, the SIA and A.G. Becker claim that the selling of third party commercial paper gives rise to the kinds of abuses and hazards identified in the Supreme Court's 1971 analysis of the Act in *Investment Company Institute* v. *Camp*, 401 U.S. 617. The Securities and Exchange Commission ("SEC") has submitted to the Board the SEC's views on the issues raised by petitioners.

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5 Under section 16, however, banks may perform certain *brokerage* activities—purchase or sale solely on the order of a customer—with respect to any securities.

Statement Regarding Petitions to Initiate Enforcement Action

A. *Commercial Paper as a "Security" under the Glass-Steagall Act*

The SIA, A.G. Becker, and the SEC advance three arguments in support of the claim that the commercial paper being sold by Bankers Trust is a "security" within the meaning of the Glass-Steagall Act: (1) commercial paper consists of marketable debt instruments and therefore constitutes an "investment security" as defined in section 16; (2) even if commercial paper is not an "investment security", commercial paper is a security because it consists of "notes" as specified in section 21; (3) commercial paper is a security for purposes of the Securities Act of 1933 and accordingly must be considered such for purposes of the Glass-Steagall Act, which was passed twenty days after the Securities Act.

Based on a review of all the relevant arguments and the facts of record, the Board is of the opinion that, as a legal matter, the stronger argument is that commercial paper is not a "security" within the intendment of the Glass-Steagall Act.

"*Investment securities.*" In interpreting the meaning of the Glass-Steagall Act, the starting point must be the language of the statute itself.[6] Although each of the four Glass-Steagall Act provisions refers to activities with regard to "securities," none of these provisions, nor any other section of that Act, contains a precise definition of the term "securities." As noted above, however, both section 16 and section 21 create a distinction between investment securities—obligations that a member bank may purchase for its own account but in general may neither underwrite nor deal in—and other securities—obligations with which banks may have no involvement (except for permissible brokerage activities).

"Investment securities" are defined in section 16 as follows:

> *marketable obligations, evidencing indebtedness* of any person, copartnership, association, or corporation in the form of bonds, notes and/or debentures *commonly*

6 *See, e.g., Transamerica Mortgage Advisers, Inc. v. Lewis*, 444 U.S. 11, 16 (1979).

> *known as investment securities under such further definition* of the *term . . . as may by regulation be prescribed by the Comptroller of the Currency.* 12 U.S.C. § 24 Seventh (emphasis added).

The Comptroller's implementing regulation defines investment security as "a marketable obligation in the form of a bond, note, or debenture *which is commonly regarded as an investment security*" that is not "predominantly speculative in nature." 12 C.F.R. § 1.3(b). (emphasis added).

The statutory language and the implementing regulation are clear: not all non-speculative, marketable debt obligations are "investment securities"; only those obligations that are *commonly known* or *regarded* as such qualify.[7] Consequently, the statute directs that the question of whether commercial paper constitutes an investment security be resolved only by resort to the common understanding of the nature of commercial paper by Congress, the regulatory agencies, and the banking industry.

The "investment securities" provision in section 16 did not originate in the Glass-Steagall Act, but in the prior provisions of the McFadden Act of 1927.[8] One of the purposes of the McFadden Act was to clarify the authority of national banks to deal in securities. At the beginning of this century, State chartered banks and trust companies, pursuant to liberal State legislation, became involved in a wide variety of investment banking functions, including the underwriting of debt and equity securities. National banks responded by expanding their activities to include the purchasing and selling—and underwriting and dealing in—not only municipal bonds but corporate bonds and stocks as well. *See* U.S. Department of the Treasury, Public Policy Aspects of Bank Securities Activities, App. 3-5 (1975). While the Comptroller permitted national banks to deal

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7 The contentions of the SIA and A.G. Becker that commercial paper is an investment security *merely* because such paper consists of marketable debt obligations ignore this plain language of the statute and the implementing regulation.

8 Pub. L. No. 639, ch. 191, 44 Stat. 1224.

in corporate debt,[9] there was no clear statutory authority for such activities. *Id.* In 1924, the Comptroller recommended legislation expressly to authorize national bank purchase and sale of investment securities.[10] The McFadden legislation followed in 1927.

Section 2 of that Act provided that the "business of buying and selling investment securities shall hereafter be limited to buying and selling without recourse" marketable debt obligations commonly known as investment securities.[11] 44 Stat. 1226. This language was intentionally framed as a reaffirmance of the existing authority of national banks with respect to investment securities rather than as an affirmative grant of new power. *See* H.R. Rep. No. 83, 69th Cong., 1st Sess. 3-4 (1926). The legislative history, however, is clear that the authority codified or confirmed by the McFadden legislation with respect to investment securities did not apply to commercial paper. This is made plain by the remarks of Congressman McFadden, the sponsor of the legislation, during debate on the bill. Mr. McFadden indicated that commercial paper is not considered an investment security (and thus would not be subject to the restrictions of the Act) but is subject to the statutory limitations on loans to individual borrowers. 67 Cong. Rec. 3232 (1926).[12]

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9 The Comptroller, as well as the courts, strictly forbade, however, national bank involvement in underwriting and dealing in equity securities. *Id.*, at 2-3, 5.

10 Annual Report of the Comptroller of the Currency for 1924, at 12.

11 This power was, of course, later restricted somewhat by the Glass-Steagall legislation.

12 The relevant colloquy involving Congressman McFadden is as follows:

> Mr. WAINRIGHT. Let me ask the gentleman whether *commercial paper, as generally understood and accepted*, is regarded as *investment security*.
>
> Mr. McFADDEN. *No; it is not*. Commercial paper comes under the limitation of section 5200 in the Revised Statutes. I never have known of commercial paper being construed as investment securities. *Id.* (emphasis added).

Statement Regarding Petitions to Initiate Enforcement Action

The view of the framers of the McFadden Act that commercial paper should be treated as a loan rather than as a security is consistent with historical studies of the commercial paper market that indicate that banks purchased and sold commercial paper (and served as commercial paper dealers) pursuant to their lending functions long before commercial banks began expanding their activities into the underwriting of corporate bonds and other debt obligations after the Civil War, activities that were restricted by the McFadden legislation concerning investment securities and, six years later, by the Glass-Steagall Act. Thus, the commercial paper activities of commercial banks were viewed as an independent operation separate from the banking industry's subsequent involvement with investment securities.[13]

Furthermore, it has been the consistent and uniform practice of the bank regulatory agencies for almost 50 years to consider commercial paper as a loan, not as an investment security. For example, the Board took the view in 1933, in letters to the House Commerce Committee and the Senate Banking Committee commenting on the proposed securities legislation of

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13 *See generally* A. Greef, The Commercial Paper House in the United States (1938) [hereinafter cited as "Greef"]; N. Baxter, The Commercial-Paper Market (1964); M. Myers, The New York Money Market, Vol. I (1932). Greef found, for example, that before 1840 commercial banks in various parts of the country were purchasing and selling commercial paper and that dealings by banks in commercial paper could be traced back to the first commercial banks organized in the United States. Greef, *supra*, at 6-7, 15-18. Indeed, by 1900 commercial banks and savings banks purchased 95 per cent of the commercial paper sold, *id.*, at 96, and commercial paper was recognized as an important form of secondary reserves for the banking system. B. Beckhart, The New York Money Market, Vol. III 236-242 (1932). In addition to purchasing commercial paper as an investment, banks participated in the selling of such paper as dealers. Greef, *supra*, at 63, 403-405; R. Foulke, The Commercial Paper Market 108 (1931). In light of the longstanding and intimate relationship of banks with commercial paper, the views of the framer of the investment security legislation that commercial paper was not subject to its provisions are consistent with common banking practice at the time.

1933, that commercial paper, "short-time paper issued for . . . obtaining funds for current transactions" and purchased by banks and corporations with temporarily idle funds should not be considered an investment security. The Board stated that the proposed legislation was apparently intended to apply only to "investment securities, which are issued for . . . obtaining capital funds . . . and are purchased by persons for investment."[14]

Although the Comptroller of the Currency is delegated primary responsibility for fashioning a definition of the term, the Comptroller has never formally ruled on the status of commercial paper as an investment security for purposes of section 16. However, in a letter to a national bank in 1971, the Comptroller's Chief Counsel took the position that commercial paper represents a loan (subject to the statutory limits on loans) and does not constitute an investment security.[15]

The present attitude of the bank regulatory agencies is consistent with the view that commercial paper is properly viewed as a loan, not as an investment security. The instructions of each of the three federal banking agencies for preparation of call reports direct that commercial paper be treated as a loan. In addition, the Federal Reserve's manual of examination procedures follows the same position. In sum, based on the views of the framers of the investment securities provisions of section 16, of the banking industry, and of the regulators, the Board believes that commercial paper has not been, and is

14 The Board's letters are reprinted in the hearings on the securities legislation. *Federal Securities Act: Hearing on H.R. 4313 before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 1st Sess. 180-181 (1933); *Securities Act: Hearings on S. 875 before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. 120 (1933).

15 Under an interpretation issued by the Comptroller, the statutory limits on loans to individual borrowers (12 U.S.C. § 84) are separate and distinct from the limit prescribed by section 16 of the Glass-Steagall Act on holding investment securities of a single issuer. 12 C.F.R. § 7.1180.

not, "commonly known" as an "investment security" and thus does not meet the statutory criteria for investment securities under section 16.

"*Securities" other than "investment securities.*" Apart from the restrictions applicable to investment securities, sections 16 and 21 impose prohibitions with respect to securities in general. Section 16 generally prohibits dealing in "securities and stock." Section 21 states that depository institutions may not engage in the business of issuing or selling "stock, bonds, debentures, *notes* or other securities." (emphasis added). Since commercial paper conventionally consists of unsecured promissory notes, it may be argued that the term "notes" as used in section 21 is, under its usual meaning, broad enough to cover commercial paper. While the words in statutes should generally be interpreted in light of their ordinary meaning,[16] it is clear for a number of reasons that the term "notes" as used in section 21 should not be interpreted according to its literal sense. First, by its terms section 21 describes depository institutions (institutions that section 21 prohibits from issuing and selling "notes") as engaged in the business of receiving deposits evidenced by a "certificate of deposit or other evidence of debt"—instruments that themselves may be classified as "notes." Thus section 21 itself expressly permits banks to issue and sell certain kinds of notes—notes evidencing deposits. Second, the Glass-Steagall Act was plainly designed to keep banks from engaging in the investment banking business, not to prohibit banks from performing the traditional functions of banks.[17] Ordinary lending transactions are evidenced by notes

16 *See, e.g., Perrin* v. *United States*, 444 U.S. 37, 42 (1979).

17 *See Investment Company Institute* v. *Camp*, 401 U.S. 617, 629 (1971) [hereinafter cited as "*ICI* v. *Camp*"]. Indeed the Supreme Court in the *Camp* case noted that commercial banks traditionally ". . . lend money, discount and negotiate promissory *notes* . . ." *Id.* (emphasis added). Indeed, if commercial paper were deemed to be a security other than an investment security, banks would be prohibited even from purchases of commercial paper for their own account, an activity that banks have long engaged in and continue to conduct. *See* Greef, *supra* note 13, at 96; Hurley, *supra* note 1, at 529.

and, in addition, banks commonly sell such notes to other lenders. It is evident that to view a note representing a bank loan as a security for Glass-Steagall Act purposes and, thus, the sale of such notes as an investment banking activity forbidden by the Act is completely at odds with the basic purpose of the Act. The rules of statutory interpretation do not require a literal reading of the term "notes" that would thwart the clear purpose of the Act and that leads to irrational results.[18]

Since the plain meaning of the statute cannot be dispositive of whether commercial paper is a security under the Glass-Steagall Act, it is appropriate to examine the history of the Act to attempt to resolve the question. It appears that Congress never adverted to bank involvement with commercial paper when it considered the Glass-Steagall legislation. There is, however, some indirect evidence that Congress did not view commercial paper, at least as the commercial paper market then existed, as the kind of obligation that would be subject to the Act. It is commonly agreed that the Glass-Steagall Act resulted from a number of specific abusive practices with respect to securities that had grown up in the banking industry. In particular, Congress was concerned about the risks and dangers to the banking system resulting from bank involvement with the "speculative operations" in securities characteristic of investment banking and with the practice of banks, begun in 1908, of establishing "security affiliates" that engaged, among other things, in underwriting bond and stock

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18 *See, e.g., Trans Alaska Pipeline Rate Cases*, 436 U.S. 631, 643 (1978). This approach has been taken by the courts in interpreting the definition of security in the securities acts, which generally define "security" to include "any note." The courts have not applied this language literally to bring all notes within the ambit of the securities laws but, on a variety of theories, have for the most part concluded that notes evidencing traditional lending transactions are not covered. *Exchange National Bank of Chicago* v. *Touche, Ross & Co.*, 544 F.2d 1126, 1131-1138 (2d Cir. 1976). *See generally United Housing Foundations, Inc.* v. *Forman*, 421 U.S. 837, 848-850 (1975).

issues. *ICI* v. *Camp*, *supra* note 17, 401 U.S. at 629-630, 632.[19] The Glass-Steagall bill was enacted only after extensive hearings on its provisions had been held in 1931 and 1932. Neither the Board nor the parties have been able to find any evidence of congressional concern about bank involvement with commercial paper. Morevoer, because at the time that the Glass-Steagall Act was being considered commercial banks purchased for their own account almost all of the commercial paper issued and commercial paper served as an important source of secondary reserves,[20] it may well be doubted that Congress could have been unaware of the extensive relationship then existing between the banking system and the commercial paper market.

Moreover, while there is no direct evidence in the legislative history of the Glass-Steagall Act on the status of commercial paper under the Act, there is evidence of contemporaneous statements by one of the draftsmen of the Act that commercial paper should not be considered a security. While the Glass-Steagall Act was pending before Congress in 1933, Congress was also considering the legislation that became the Securities Act of 1933. During Senate consideration of the securities bill, Senator Glass, the chief architect of the prohibitions against bank securities activities, proposed that short-term notes, including "9 months' commercial paper," be excluded from the definition of securities contained in that bill because to define such obligations as securities would "radically interfere" with "ordinary commercial banking transactions."[21] While Senator

19 *See also Russell* v. *Continental Illinois National Bank & Trust Co.*, 479 F.2d 131 (7th Cir.), *cert. denied*, 414 U.S. 1040 (1973); *Baker, Watts & Co.* v. *Saxon*, 261 F. Supp. 247 (D.D.C. 1966), *aff'd sub nom. Port of New York Authority* v. *Baker, Watts & Co.*, 392 F.2d 497 (D.C. Cir. 1968); *New York Stock Exchange, Inc.* v. *Smith*, 404 F. Supp. 1091 (D.D.C. 1975), *rev'd on other grounds*, 562 F.2d 736 (D.C. Cir. 1977), *cert. denied*, 435 U.S. 942 (1978).

20 *See* note 13 *supra*.

21 *Securities Act: Hearings on S. 875 before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. 98 (1933).

Glass's proposed amendment was eventually adopted only as an exemption from some of the substantive provisions of the Securities Act,[22] his statements concerning the need for such an amendment strongly suggest that one of the principal draftsmen of the Glass-Steagall Act viewed commercial paper as closely linked to "ordinary commercial banking transactions" and not as involving the speculative investment banking functions that the legislation he sponsored was intended to restrain.[23]

In the course of administering the Glass-Steagall Act over the years the Board has not applied the Glass-Steagall Act prohibitions to the activities of banking organizations with respect to commercial paper. As noted above in the discussion of investment securities, the Board has traditionally viewed commercial paper purchased for a bank's own account as a loan, not as a security, for purposes of call reports. Furthermore, in its 1973 interpretation of the Glass-Steagall Act with respect to the sale of thrift notes (small denomination unsecured notes sold more or less continuously) by bank holding companies, the Board, while not expressly finding that commercial paper is not a security, stated that the issuance of commercial paper by a bank holding company "is not an activity intended to be included within the scope of section 20 of the Glass-Steagall Act." 12 C.F.R. § 250.221.

In addition to a review of the legislative history and agency interpretation, it is also appropriate to consider the status of commercial paper under the Act in light of the purposes for

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22 The effect of this action by Congress is discussed below.

23 The SEC argues that the testimony of Senator Glass is not persuasive because the Securities Act was enacted *before* the Glass-Steagall Act. Thus, according to the SEC, Senator Glass, if he really believed commercial paper was not a security, would have attempted, after a broad definition of "security" was adopted in the Securities Act, to amend the Glass-Steagall Act to exclude commercial paper. However, this argument assumes, without any support, that Senator Glass viewed the Securities Act definitions as germane to the Glass-Steagall Act.

which the Act was passed—to separate commercial and investment banking. As noted above with respect to the definition of "notes", a broad generic or literal reading of the term "security" would likely encompass a number of instruments that banks routinely deal with in the course of their business and would, consequently, be contrary to the basic purpose of the Act. On the other hand, a highly technical or formalistic approach might permit evasions of the mandate of Congress. However, it would seem that if a particular kind of financial instrument evidences a transaction that is more functionally similar to a traditional commercial banking operation than to an investment transaction, then fidelity to the purposes of the Act would dictate that the instrument should not be viewed as a security.

If such an approach is taken with respect to commercial paper, the Board believes that the stronger conclusion is that commercial paper currently being sold by Bankers Trust represents a financing transaction that is closer in function to commercial lending than to the sale of an investment. Historically, the dividing line between commercial and investment banking depended on whether short-term or long-term funds were being provided. As a short-term instrument, commercial paper fell on the commercial banking side of the line. Historical studies of the commercial paper market indicate that, as that market originated and developed, commercial paper was the functional equivalent of a bank loan. Commercial paper was used to raise funds for short-term needs and was sold almost exclusively to commercial banks.

It is clear, however, that the commercial paper market has changed somewhat in recent years. Most notably, commercial banks are no longer the predominant purchasers of commercial paper.[24] Nevertheless, the Board is of the opinion that, after a review of Bankers Trust's activities, the commercial paper currently being sold by the bank appears to evidence transactions that are more like commercial lending transactions than the sale of investments. First, the commercial paper sold

24 *E.g.*, Hurley, *supra* note 1, at 529.

by Bankers Trust, like commercial paper generally, is a short-term instrument. While it may no longer be said that the provision of short-term credit to business is exclusively the function of banks, short-term loans continue to be the principal activity of commercial banks.[25] In addition, a typical commercial loan transaction involves a borrower and a single lender or, in the case of a loan participation, a relatively small number of lenders, that regularly extend credit as part of a business. Likewise, the purchasers of the commercial paper sold by Bankers Trust are relatively few in number and purchase paper in denominations larger than an average investor might be expected to afford. Moreover, it appears that most of the purchasers of the paper are part of the bank's base of institutional customers that purchase short-term obligations on a regular basis. These facts, in the Board's view, support the conclusion that the commercial paper currently being sold by Bankers Trust is more analogous to a commercial loan than to an investment. This view is consistent with the legislative history of the Glass-Steagall Act and the Board's general approach to commercial bank involvement with commercial paper. Accordingly, the Board believes that the stronger argument is that commercial paper should not be considered a security for the purposes of the Glass-Steagall Act.[26]

The Securities Act of 1933. The SIA, A.G. Becker, and the SEC argue that because commercial paper is a security for purposes of the Securities Act of 1933,[27] commercial paper

25 While it is the practice of commercial paper issuers to reissue (roll over) paper at maturity, the purchasers of the paper, unlike the holders of bonds or other longer term instruments, have the legal right to demand payment at the original maturity date.

26 The Board's conclusion is limited to the obligations generally recognized as commercial paper: prime quality, negotiable, usually unsecured, promissory notes with maturities less than nine months that are exempt from the registration requirements of the Securities Act of 1933. The Board expresses no opinion with regard to the sale by a bank of third party obligations that do not meet these criteria.

27 Act of May 27, 1933, ch. 38, 48 Stat. 74.

must likewise be viewed as a "security" under the Glass-Steagall Act. Under section 2(1) of the Securities Act, 15 U.S.C. § 77b(1), the term "security" includes "any note." Section 3(a)(3) of that Act exempts from the registration and prospectus-delivery requirements of the Act any note the proceeds of which are used for current transactions and with a maturity of nine months or less. 15 U.S.C. § 77c(a)(3). Under sections 12(2) and 17(c), 15 U.S.C. §§ 77l(2), 77q(c), such short-term notes are not exempt from the antifraud prohibitions of that Act. Consequently, it is generally held that commercial paper is a security (albeit an exempt security) for purposes of the Securities Act.[28] The petitioners and the SEC contend that the Securities Act definition of "security" should be read into the Glass-Steagall Act because the two pieces of legislation address the same activities and were enacted within three weeks of each other in 1933.[29]

28 *Franklin Savings Bank* v. *Levy*, 551 F.2d 521, 524 n.6 (2d Cir. 1977). With respect to the status of commercial paper under the other major federal securities law, the Securities Exchange Act, the question is not as clear. Unlike the 1933 Act, the 1934 Act expressly exempts commercial paper from that Act's *definition* of security. 15 U.S.C. § 78c(a)(10). The courts have not applied the exclusion literally, and courts have found that commercial paper is covered under the 1934 Act, at least where the particular commercial paper involved did not meet the criteria for exemption from registration under the 1933 Act, *e.g.*, the commercial paper was sold to the public. *Sanders* v. *John Nuveen & Co.*, 463 F.2d 1075, 1078-1080 (7th Cir.), *cert. denied*, 409 U.S. 1009 (1972).

29 Petitioners and the SEC rely on the legal analysis contained in a 1977 Board staff study of commercial bank private placements, which concluded that the definitions of "issue", "underwriter", and "distribution" in the Securities Act were "a compelling analogy" to the same terms employed in the Glass-Steagall Act. The Board has never formally reviewed the legal conclusions of the staff's private placement study. However, the private placement legal analysis does not necessarily contradict the position taken here. The private placement conclusions do not suggest that the definitions of the Securities Act are *conclusive*. In addition, the Board believes there is a distinction between definitions of activities carried on in the securities business and the definitions of a security, which are jurisdictional in nature and more closely linked to the purposes for which each Act was enacted.

Statement Regarding Petitions to Initiate Enforcement Action

While it seems clear that the definition of security in the Securities Act is relevant to a determination with regard to what instruments Congress thought were securities covered by the Glass-Steagall Act, it is the Board's opinion that the definition of security in the federal securities laws cannot be deemed conclusive for Glass-Steagall Act purposes. In the Board's view, this conclusion is supported by a number of arguments, but the most persuasive argument is that the definition of security under the Securities Act encompasses a variety of instruments that represent traditional banking functions and that to apply the prohibitions of the Glass-Steagall Act to such obligations would make illegal functions that clearly are properly part of the business of banking.[30] For example, a bankers' acceptance, like commercial paper, is a security under the Securities Act but exempt from registration. 15 U.S.C. §§ 77b(1), 77c(a)(3). However, commercial banks routinely purchase and sell bankers' acceptances and commercial banks (including Bankers Trust) serve as dealers in bankers' acceptances. Indeed, the Board determined as long ago as 1934 that bankers' acceptances were *not* securities under the Glass-Steagall Act.[31] To view the Securities Act definition of security as conclusive for Glass-Steagall purposes, as the securities industry representatives and the SEC suggest, would require that the traditional activities of commercial banks regarding bankers' acceptances be considered as the prohibited dealing in securities. This result is clearly contrary to the intent of the Glass-Steagall Act, which was not intended to restrict commercial banking functions. *ICI* v. *Camp*, *supra* note 17, at 629. In addition, although the courts are not unanimous, the

30 It should also be noted that the Securities Act and the Glass-Steagall Act were not enacted to accomplish the same objectives. The Securities Act is an *investor* protection measure; the Glass-Steagall act is designed to protect *banks*, not investors. *Russell* v. *Continental Illinois National Bank & Trust Co.*, *supra*, note 19.

31 Letter, dated June 8, 1934, from the Secretary of the Board to the Federal Reserve Agent, Federal Reserve Bank of New York.

securities laws have in some cases been held applicable to certificates of deposits issued by banks,[32] passbook savings accounts,[33] loan participations,[34] and bills of exchange.[35] Under the theory advanced by the SIA, A.G. Becker, and the SEC, banks would be prohibited from issuing,[36] selling, or dealing in each of these instruments on the grounds that doing so is the prohibited business of investment banking. The Board does not believe such contentions are consistent with the purpose of the Act.[37]

32 *Garner* v. *Pearson*, 374 F. Supp. 591, 596 (M.D. Fla. 1974).

33 *SEC* v. *First American Bank & Trust Co.*, 481 F.2d 673, 678 (8th Cir. 1973).

34 *Lehigh Valley Trust Co.* v. *Central National Bank of Jacksonville*, 409 F.2d 989, 991-992 (5th Cir. 1969).

35 *MacAndrew & Forbes Co.* v. *American Barmag Corp.*, [1972-1973 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,532 (D.S.C. 1972).

36 The SEC states that considering time deposits as securities under the Glass-Steagall Act would not disrupt the statutory scheme of that Act because the Act does not prohibit a bank from issuing its *own* securities—only dealing in or underwriting the securities issued by *others*. However, section 21 plainly prohibits banks from engaging in the business of "issuing" and "selling" securities and does not limit such securities to those of third parties. While Board staff has taken the position that a bank's occasional issuance of its own stock, bonds, or debentures (an activity essential to the viability of the organization) does not constitute being engaged "in the business" of issuing securities under section 21, it seems clear that banks issue and sell time deposits, bankers' acceptances, and similar instruments as a regular part of their "business" and, if such instruments are considered securities for Glass-Steagall Act purposes, banks would be prohibited by the Act from such activities.

37 The Board expresses no opinion regarding the legal status of the commercial paper sold by Bankers Trust under the Securities Act of 1933 or under any other law except the Glass-Steagall Act. It is noted, however, that commercial paper has been held to be a security for at least some purposes under the federal securities laws. *See* pages 136A-137A, *supra*.

Statement Regarding Petitions to Initiate Enforcement Action

Because of the historical involvement of the banking industry with commercial paper, the nature of the commercial paper currently sold by Bankers Trust, and the fact that commercial paper is exempt from the substantive obligations of the Securities Act of 1933 (except for the antifraud provisions), the Board concludes that, notwithstanding the status of commercial paper as an exempt security under the Securities Act, the stronger argument is that commercial paper is not a security for purposes of the Glass-Steagall Act.

B. *Bankers Trust's Activities as Dealing in or Underwriting Securities*

Since, in the Board's opinion, the stronger argument is that commercial paper should not be treated as a security covered by the Glass-Steagall Act, the restrictions of the Act with regard to issuing, underwriting, selling, and dealing in securities do not apply. Thus, it is not necessary to reach the issue of whether the activities engaged in by Bankers Trust are prohibited by the Act.

C. *Policy Concerns Behind the Glass-Steagall Act*

The SIA, A.G. Becker, and the SEC also assert that the selling of commercial paper by Bankers Trust produces the same kinds of risks to the bank and potential for conflicts of interest that Congress intended to eliminate in enacting the Glass-Steagall Act. In its opinion on the Glass-Steagall Act in *ICI* v. *Camp*, *supra* note 17, the Supreme Court analyzed the scope of the Act in terms of specific "hazards" and "financial dangers" that Congress had in mind when banks engaged in activities prescribed by the Act. 401 U.S. at 630.

At the outset, the Board notes that since the stronger view is that commercial paper should not be considered a security for Glass-Steagall Act purposes, the sale of commercial paper by Bankers Trust is not prohibited by the specific terms of that Act. Accordingly, it does not appear necessary to examine the dangers that the Act was intended to eliminate.[38] Nevertheless,

38 *See Aaron* v. *SEC*, 100 S. Ct. 1945, 1955 (1980).

the Board believes that the sale of third party commercial paper by a commercial bank could involve, at least in some circumstances, practices that are not consistent with principles of safe banking.[39] Thus, the Board, in cooperation with the other federal bank regulatory agencies, has initiated the process of developing guidelines governing the sale of third party commercial paper by a commercial bank designed to prevent potential unsafe or unsound practices that could arise in such an activity. When these guidelines are developed and submitted to the Board for consideration, the Board will address in that proceeding the general issues raised by the allegations of petitioners and the SEC relating to potential undue risks to banks or conflicts of interest arising from this activity.

Public Policy Considerations

A.G. Becker advances a number of public policy considerations that it claims militate against permitting a commercial bank to sell third party commercial paper. A.G. Becker first asserts that a full-service commercial bank selling commercial paper enjoys unfair competitive advantages over nonbank sellers because banks would be able to offer a package of services to an issuer of commercial paper that the nonbank seller could not offer. A.G. Becker also cites the potential for predatory pricing, access as settlement agent to the customer lists of competing sellers, and the cut-off of credit to nonbank sellers of commercial paper.[40] The Board's review of Bankers Trust's current operations in selling commercial paper has not uncovered any evidence at this time of such alleged unfair competitive practices.

It is next claimed that persons classified as "brokers" under the Securities Exchange Act of 1934 are subject to a number of

39 *See* 12 U.S.C. § 1818(b).

40 A.G. Becker claims that the asserted advantages constitute "unfair practices" by banks under section 18(f) of the Federal Trade Commission Act and the Board's Regulation AA. 12 C.F.R. § 227.

regulatory requirements designed to protect investors and that banks (which are exempt from the definition of broker in the Securities Exchange Act) are not subject to similar restrictions. However, since commercial paper is exempted from the definition of security in the Securities Exchange Act,[41] it would appear that a nonbank seller of commercial paper is not subject to the provisions of that Act if commercial paper is the only instrument sold. In any event, commercial banks are subject to certain investor protection requirements in connection with their securities transaction activities similar to those imposed on nonbank brokers. *E.g.*, C.F.R. § 208.8(k). Moreover, Bankers Trust sells commercial paper only to sophisticated institutional investors that would appear to be less in need of many of the safeguards designed to protect average investors.

Finally, A.G. Becker claims that if commercial banks become dominant in the commercial paper market, the resulting competition may reduce the efficiency of the securities industry and impair the capital-raising mechanism provided by that industry. Presently, however, Bankers Trust is by no means dominant in the commercial paper market and there is no available evidence of disruption of the capital markets as a result of Bankers Trust's activities. Accordingly, the Board believes that the policy considerations advanced by A.G. Becker do not at this time warrant prohibition of Bankers Trust's selling of third party commercial paper.

In summary, the Board has determined to deny the petitions of the SIA and A.G. Becker to the extent such petitions allege that Bankers Trust's commercial paper activities violate the Glass-Steagall Act or that such activities should be prohibited by general considerations of public policy. The Board is taking no action regarding petitioners' contentions of dangers to Bankers Trust and potential conflicts of interest and will consider these issues in the context of the Board's consideration of guidelines governing the sale of third party commercial paper by commercial banks.

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41 15 U.S.C. § 78c(a)(10).

Statement Regarding Petitions to Initiate Enforcement Action

Request for Oral Argument

Counsel for A.G. Becker has requested the opportunity to present oral argument to the Board when this matter is submitted to the Board for consideration. However, the Board as yet has initiated no agency proceedings in connection with Bankers Trust's commercial paper activities and A.G. Becker is not a party to any agency proceeding pending before the Board. The Board notes that counsel for A.G. Becker has met with the Board's staff on at least two occasions concerning the activities of Bankers Trust. Moreover, the Glass-Steagall Act issues resolved by the Board are essentially legal in nature and all the interested organizations have submitted extensive written arguments on these issues. In the Board's view, these written submissions adequately explain the issues involved and oral argument before the Board at this time would serve no useful purpose. Accordingly, the request by A.G. Becker for oral argument before the Board on this matter is denied.

Letter, dated October 16, 1980, from Theodore E. Allison to Harvey L. Pitt

OCT 16 1980

Harvey L. Pitt, Esq.
Fried, Frank, Harris, Shriver
& Kampelman
600 New Hampshire Avenue, N.W.
Washington, D.C. 20037

Dear Mr. Pitt:

This is in response to the "Application for Stay" submitted by A.G. Becker Incorporated ("A.G. Becker") dated October 2, 1980, with respect to the Board's letter and statement, dated September 26, 1980, regarding the petition of A.G. Becker that the Board prohibit Bankers Trust Company ("Bankers Trust") from selling commercial paper of issuers not related to the bank ("third party commercial paper"). The Board's letter and statement denied A.G. Becker's petition and the similar petition of the Securities Industry Association (the "SIA") to the extent the petitions allege that Bankers Trust's activities violate the Glass-Steagall Act or that such activities should be prohibited by general considerations of public policy. However, noting that the sale of third party commercial paper by a bank could involve, at least in some circumstances, unsafe or unsound banking practices, the Board took no action on petitioners' contentions of dangers to Bankers Trust and potential conflicts of interest arising from such activities, pending the Board's consideration of these issues in the context of its consideration of general guidelines, developed in cooperation with the other bank regulatory agencies, designed to prevent unsafe or unsound practices in the sale of commercial paper by a bank.

A.G. Becker requests that the Board immediately issue an order prohibiting Bankers Trust "and all of the member banks" from selling commercial paper until either a court resolves the propriety of the Board's action or the Board implements guidelines to prevent unsafe or unsound practices.

A.G. Becker states that this action is necessary because such guidelines may not be implemented until after the nation's commercial banking system has been exposed to substantial injury as a result of unsafe or unsound practices in the sale of commercial paper.

The Board does not interpret A.G. Becker's petition as an application for a stay, in the usual sense, of an agency action, since the Board's action of September 26, 1980, with respect to Bankers Trust's commercial paper activities constitutes no authorization for any activities and imposes no requirements or disabilities on any person. The Board's action did not authorize Bankers Trust (or any other bank) to engage in any activities. Bankers Trust is organized under the laws of the State of New York and the scope of its authority to engage in the banking business is determined in the first instance by those laws. In its action of September 26, the Board merely determined that the Board would not at this time initiate enforcement proceedings against Bankers Trust to prevent the challenged activities on the basis of some (but not all) of the grounds advanced in the petitions of A.G. Becker and the SIA. The postponement or stay of the effectiveness of such a decision not to take action would not appear to have any practical meaning in terms of the rights of the interested organizations.

A.G. Becker appears, rather, to be requesting special interim relief prohibiting all commercial paper activities by member banks pending implementation of the proposed guidelines or judicial review, based on the Board's finding that the sale of commercial paper may involve at least in some circumstances unsafe or unsound banking practices. In the Board's view, such relief is not within the Board's authority and is not warranted. With respect to preventing unsafe or unsound banking practices, the Board's authority under the Financial Institutions Supervisory Act is limited to State-chartered member banks. The Board has no cease-and-desist authority over national banks. 12 U.S.C. §§ 1813(q), 1818(b)(1).

Letter, dated October 16, 1980

While the Board is concerned about possible unsafe or unsound practices that could be involved in Bankers Trust's commercial paper activities and in similar activities by any other State member bank that commences such activities prior to implementation of the guidelines, the Board does not believe that any possible unsafe or unsound practice that might be involved in Bankers Trust's present selling activities poses an immediate threat to the safety of the bank or to its depositors. This finding is based on the Board's review of all of Bankers Trust's practices in selling commercial paper during the Board's consideration of the petitions of A.G. Becker and the SIA and on the fact that any undue risks that might be involved in the bank's commercial paper operations are not substantial in relation to the bank's total resources. Moreover, the activities of State member banks other than Bankers Trust were not challenged by A.G. Becker and it does not appear that other State member banks plan imminently to initiate selling third party commercial paper on a significant scale. Finally, the procedure for developing guidelines for the sale of third party commercial paper has already been initiated and the Board expects to consider such guidelines without undue delay.

For the above reasons, the Board has determined to deny A.G. Becker's request for an immediate Board order prohibiting Bankers Trust and all other member banks from selling third party commercial paper pending judicial review of the Board's action on A.G. Becker's petition or pending implementation of guidelines to prevent unsafe or unsound practices.

Very truly yours,

(signed) THEODORE E. ALLISON
Theodore E. Allison
Secretary of the Board

RMA:gjr
10/16/80

SIA Complaint for Declaratory Judgment, Injunctive and Other Relief, in Civil Action No. 80-2730 (D.D.C., filed October 24, 1980)

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION, 20 Broad Street, New York, N.Y., (212) 425-2700,

Plaintiff,

—v.—

THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, Federal Reserve Building, Constitution Avenue, N.W., Washington, D.C. 20551,

—and—

PAUL A. VOLCKER, as Chairman of the Board of Governors of the Federal Reserve System, Federal Reserve Building, Constitution Avenue, N.W., Washington, D.C. 20551,

—and—

FREDERICK H. SCHULTZ, NANCY H. TEETERS, J. CHARLES PARTEE, HENRY C. WALLICH, EMMET J. RICE, LYLE E. GRAMLEY, as Members of the Board of Governors of the Federal Reserve System, Federal Reserve Building, Constitution Avenue, N.W., Washington, D.C. 20551,

Defendants.

COMPLAINT FOR DECLARATORY JUDGMENT AND INJUNCTIVE AND OTHER RELIEF

Plaintiff, by its attorneys, brings this action against the above-named defendants and alleges:

Complaint

Jurisdiction and Venue

1. This is a civil action for declaratory judgment and injunctive and other relief. It arises under various sections of the Banking Act of 1933, as amended (herein referred to as the "Glass-Steagall Act"), codified in various sections of Title 12 of the United States Code, and the regulations thereunder; the Federal Reserve Act of 1913, 12 U.S.C. §§ 221 *et seq.*, and the regulations thereunder; the Federal Deposit Insurance Corporation Act, as amended, 12 U.S.C. §§ 1811, *et seq.*, and the regulations thereunder; the Declaratory Judgment Act, 28 U.S.C. §§ 2201 and 2202; and the Administrative Procedure Act, 5 U.S.C. §§ 701 *et seq.*. Jurisdiction is conferred on this Court by 28 U.S.C. §§ 1331. Venue lies in this district pursuant to 28 U.S.C. § 1391. There exists between the plaintiff and the defendants an actual controversy, justiciable in character, in respect of which plaintiff requires a determination of its rights by this Court. The amount in controversy exceeds ten thousand dollars ($10,000).

2. Because of uncertainty concerning the appropriate forum for review of the Board's action, and in order to preserve its rights, plaintiff is filing a Petition for Review of the Board's action in the United States Court of Appeals for the District of Columbia Circuit simultaneously with this Complaint.

Parties

3. Plaintiff Securities Industry Association (herein referred to as the "SIA") is an association incorporated in the State of Delaware and having its principal place of business in the City of New York in the State of New York and having an office in Washington, D.C. The SIA is a national trace association representing approximately 500 organizations responsible for over 90 percent of the securities brokerage and investment banking business of the nation, for which it sues in a representative capacity. Its membership is a cross section of the securities industry: the business of its members includes, *inter alia*,

retail and institutional brokerage, over-the-counter market making, underwriting and other investment banking activities and the distribution and trading of commercial paper and other securities. The firms which comprise the SIA's membership are located across the nation and provide services to investors of every size and type.

4. Defendant Board of Governors of the Federal Reserve System (herein referred to as the "Federal Reserve Board" or the "Board") is an agency of the United States Government, created by the Federal Reserve Act of 1913, 12 U.S.C. §§ 221 *et seq.*, and charged with the responsibility of administering, enforcing and regulating the nation's banking system in accordance with, *inter alia*, various provisions of Title 12 of the United States Code, including various provisions of the Glass-Steagall Act and the Federal Deposit Insurance Corporation Act. The Board is an "agency" within the meaning of the Administrative Procedure Act, 5 U.S.C. § 551(2). Defendant Volcker is Chairman of the Board; defendants Schultz, Teeters, Partee, Wallich, Rice, and Gramley are individual members of the Board, and are named as defendants herein in such capacities.

Statutory Framework

5. The Glass-Steagall Act was enacted in 1933 in response to the collapse of the commercial banking system during the Great Depression. Congress perceived that crisis to have been caused in large part by the abuses stemming from bank involvement in the securities business, and the Glass-Steagall Act was designed to remedy these abuses by divorcing commercial banking from investment banking.

6. Section 16 of the Glass-Steagall Act, 12 U.S.C. § 24 Seventh, limits the business of dealing in securities and stock by any national bank "to purchasing and selling such securities and stock without recourse, solely upon the order, and for the

account of, customers, and in no event for its own account. . . ." Such banks are also expressly prohibited from "underwrit[ing] any issue of securities or stock". The provisions of Section 16 are made applicable to state member banks by Section 5(c) Fifth of the Glass-Steagall Act, 12 U.S.C. § 335.

7. Section 21 of the Glass-Steagall Act, 12 U.S.C. § 378, makes it unlawful for any person or financial institution "engaged in the business of issuing, underwriting, selling, or distributing . . . stocks, bonds, debentures, notes or other securities, to engage at the same time to any extent whatever in the business of receiving deposits" except to the extent permitted to national banking associations by Section 16 of the Glass-Steagall Act.

8. Section 8 of the Federal Deposit Insurance Corporation Act, 12 U.S.C. § 1818, empowers the Federal Reserve Board to institute cease-and-desist proceedings against any "insured bank" which has violated or is about to violate any federal laws, rules or regulations or which has engaged or is about to engage in unsafe or unsound banking practices.

The Board's Action

9. On information and belief, on or before July 26, 1978, Bankers Trust Company ("Bankers Trust"), a state member bank of the Federal Reserve System and an "insured bank" within the meaning of the Federal Deposit Insurance Corporation Act, 12 U.S.C. §§ 1811 *et seq.*, began a new program of underwriting, selling and dealing in commercial paper and distributing such securities to the public. On information and belief, Bankers Trust since that time has engaged in such underwriting, selling, and dealing in commercial paper and has purchased in the secondary market commercial paper of issuers for which it has acted as underwriter, seller and dealer. In doing so Bankers Trust has placed itself in competition with the members of the SIA active in the commercial paper business.

Complaint

10. During November 1978 the SIA became aware that the Federal Reserve Board was engaged in a study of the distribution of commercial paper by Bankers Trust. As a member bank, Bankers Trust is subject to the regulatory supervision of the Board, and as an insured bank, it is subject to cease-and-desist proceedings which may be instituted by the Federal Reserve Board in respect of its operations.

11. On January 31, 1979, the SIA submitted to the Board's General Counsel a memorandum discussing the propriety and permissibility of commercial paper distribution activities by member banks and pointing out that, as a matter of law, the commercial paper activities of Bankers Trust violate the Glass-Steagall Act. On June 28, 1979 the General Counsel of the Board issued an opinion in which he concluded that, with certain limited exceptions, the sale of commercial paper by a commercial bank such as Bankers Trust was not prohibited by the Glass-Steagall Act. On July 26, 1979 the SIA filed an Application for Review with the Board which supplemented its memorandum of January 31, 1979 and requested the Board, among other things, formally to review the commercial paper activities of Bankers Trust and to order Bankers Trust to cease and desist from all its third party commercial paper activities.

12. On September 26, 1980 the Board denied the petition filed by the SIA. The Board stated that the issues involved were "primarily legal" in nature and based its action on its stated legal determination that "the financing instrument commonly known as commercial paper is not a 'security' within the meaning of the Glass-Steagall Act."

13. The Board's action constituted a final disposition of the proceedings instituted by the SIA concerning the commercial paper activities of Bankers Trust and constituted final agency action within the meaning of the Administrative Procedure Act.

Complaint

14. On October 16, 1980, the SIA submitted to the Board an application in the form of a letter stating its intention to seek prompt review of the Board's decision in federal court and requesting that the Board immediately stay the effectiveness of its September 26, 1980 action until a court resolves the propriety of the Board's action and the activities of Bankers Trust. To date the Board has failed to grant this request.

Violation of the Federal Banking Laws

15. The activities engaged in by Bankers Trust constitute underwriting, selling and dealing in securities in violation of Sections 16 and 21 of the Glass-Steagall Act and as a matter of law constitute unsafe or unsound banking practices.

16. The Board's action of September 26, 1980 was arbitrary, capricious, an abuse of discretion, not in accordance with law, without any rational basis, and in excess of its statutory authority in that it was based solely on an erroneous legal conclusion and purports to sanction the illegal commercial paper activities of Bankers Trust and other similarly situated banks.

17. The illegal action of the Board, and the illegal activities on the part of Bankers Trust which it purports to sanction, will have an immediate and deleterious effect on the members of the SIA and on the public at large. The members of the SIA, for which it sues in a representative capacity, will suffer present and continuing serious and irreparable injury as a direct result of the unlawful activities authorized thereby. This illegal activity will subject the SIA's members to unlawful competition, will deprive them of legitimate business, and will dilute, divert and withdraw a substantial portion of the potential market for third party commercial paper to the substantial and irreparable injury of such members of the SIA. Moreover, the Board's action and the illegal activities of Bankers Trust will contribute to precisely those dangers against which the Glass-Steagall Act was originally directed.

18. The members of the SIA—which are all themselves subject to prohibitions of the Glass-Steagall Act preventing them from expanding their operations into the commercial banking business—are directly interested and aggrieved parties entitled to review and challenge this action of the Federal Reserve Board. The SIA has exhausted the administrative remedies available to it, has no adequate remedy at law and has no means available to it to protect the rights infringed by the Board's action other than the present action. Plaintiff SIA, and its members for which it sues in its representative capacity, will be permanently and irreparably harmed if the Court does not grant the relief prayed for herein.

WHEREFORE, plaintiff prays:

1. That this Court declare invalid the Board's determination and ruling that as a matter of law commercial paper is not a "security" within the meaning of the Glass-Steagall Act and that the Glass-Steagall Act does not prohibit member banks from underwriting, selling or dealing in commercial paper;

2. That this Court declare invalid the refusal of the Board to institute cease-and-desist proceedings and to issue a cease-and-desist order against Bankers Trust in connection with its commercial paper activities;

3. That this Court hold unlawful and set aside the action of the Board dated September 26, 1980;

4. That this Court enjoin defendants and their successors to set aside and withdraw the Board's action;

5. That this Court enjoin defendants and their successors immediately to institute cease-and-desist proceedings against Bankers Trust and any and all other member banks engaging in or about to engage in similar illegal commercial paper activities; and

6. That this Court grant such other and further relief as may be appropriate.

Respectfully submitted,

/s/ JOHN M. LIFTIN
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SIA Petition for Review in Civil Action No. 80-2314 (D.C. Cir., filed October 24, 1980)

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Civil Action No. 80-2314

SECURITIES INDUSTRY ASSOCIATION,

Petitioner,

—v.—

THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,

—and—

PAUL A. VOLCKER, as Chairman of the Board of Governors of the Federal Reserve System,

—and—

FREDERICK H. SCHULTZ, NANCY H. TEETERS, J. CHARLES PARTEE, HENRY C. WALLICH, EMMET J. RICE, LYLE E. GRAMLEY, as Members of the Board of Governors of the Federal Reserve System,

Respondents.

PETITION FOR REVIEW

The Securities Industry Association hereby petitions this Court to stay, enjoin, set aside, suspend, modify or otherwise review an order of the Board of Governors of the Federal Reserve System dated September 26, 1980, for such other and further relief as may be just, necessary and appropriate, and for any further relief as may be just, necessary and appropriate in aid of the jurisdiction of this Court.

Because of uncertainty concerning the appropriate forum for review of the Board's action, petitioner is filing simultaneously with this Petition for Review a Complaint in the United States District Court for the District of Columbia naming as defendants the respondents herein.

The Securities Industry Association is a national trade association whose members are engaged in the securities brokerage and investment banking business.

The order of the Board is attached hereto as Exhibit A.

Respectfully submitted,

/s/ JOHN M. LIFTIN
John M. Liftin
James B. Weidner
Janet R. Zimmer
Thomas M. Shoesmith

Rogers & Wells
1666 K Street, N.W.
Washington, D.C. 20006
(202) 331-7760

Of Counsel:

William J. Fitzpatrick
Securities Industry Association
20 Broad Street
New York, N.Y.
(212) 425-2700

Donald J. Crawford
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490 L'Enfant Plaza East, S.W.
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Defendants' Motion to Dismiss or, in the Alternative, for Summary Judgment, filed in Civil Action No. 80-2730 (D.D.C.)

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al., 20th and Constitution Avenue, N.W., Washington, D.C. 20551, Telephone: (202) 452-3000,

Defendants.

DEFENDANTS' MOTION TO DISMISS OR, IN THE ALTERNATIVE, FOR SUMMARY JUDGMENT

Pursuant to Rule 12(b)(1), Federal Rules of Civil Procedure, defendants, by their undersigned counsel, hereby move to dismiss this action on the grounds that the Court lacks jurisdiction over the subject matter of the action. In the alternative, defendants move for summary judgment pursuant to Rule 56(b), Federal Rules of Civil Procedure, on the ground that there are no genuine issues of material fact and defendants are entitled to judgment as a matter of law.

In support of their motion, defendants respectfully refer the Court to the attached Memorandum of Points and Authorities

in Support of Defendants' Motion to Dismiss or, in the Alternative, for Summary Judgment, and the Exhibit thereto.

Respectfully submitted,

NEAL L. PETERSEN
General Counsel

JAMES V. MATTINGLY, JR.
Assistant General Counsel

/s/ RICHARD M. ASHTON

RICHARD M. ASHTON
Attorney
Board of Governors of the
Federal Reserve System
20th and Constitution Avenue, N.W.
Washington, D.C. 20551
(202) 452-3750

Counsel for defendants.

DATED: January 19, 1981

Defendants' Statement of Material Facts As to Which There is No Genuine Issue filed in Civil Action No. 80-2730 (D.D.C.)

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,

Defendants.

DEFENDANTS' STATEMENT OF MATERIAL FACTS AS TO WHICH THERE IS NO GENUINE ISSUE

Pursuant to Rule 1-9(h) of this Court, defendants hereby set forth in support of their motion, in the alternative, for summary judgment the following statement of material facts as to which there is no genuine issue in this suit:

1. During 1978, Bankers Trust Company, New York, New York ("Bankers Trust"), a State-chartered member bank of the Federal Reserve System, began selling commercial paper issued by corporations not related to the bank ("third party commercial paper"). (R.6,9).*

* "R. __" refers to the administrative record maintained by the Board with respect to the petitions of Becker and the SIA concerning Bankers Trust's commercial paper activities. A copy of the record has been filed with the Court.

Defendants' Statement of Material Facts

2. In November 1978, A.G. Becker Incorporated ("Becker") and the Securities Industry Association (the "SIA") expressed concern to the staff of the Board of Governors of the Federal Reserve System (the "Board") regarding the legality of Bankers Trust's commercial paper activities. (R.6).

3. On June 29, 1979, after meetings between Board staff and the representatives of Becker and the SIA and after numerous written submissions by Becker, the SIA, Bankers Trust, and the General Counsel of the Securities and Exchange Commission (R.116-279, 283-320, 323-327, 329-335), the Board's General Counsel issued an opinion concluding that commercial banks may, subject to certain limitations, sell third party commercial paper. (R.336-361).

4. By letters to Becker and the SIA dated June 29, 1979, the Board's General Counsel stated that, at the request of either organization, he would recommend that the Board review his opinion. (R.360-361).

5. In submissions dated July 26, 1979, and January 31, 1980, respectively, the SIA and Becker requested that the Board review the General Counsel's opinion and initiate formal adjudicatory proceedings to restrain Bankers Trust's activities. (R.363-414, 554-558).

6. On September 26, 1980, the Board issued the attached statement and letter with respect to the petitions of Becker and the SIA. (R.662-692).

Respectfully submitted,

NEAL L. PETERSEN
General Counsel

JAMES V. MATTINGLY, JR.
Assistant General Counsel

/s/ RICHARD M. ASHTON

RICHARD M. ASHTON
Attorney
Board of Governors of the
Federal Reserve System
Washington, D.C. 20551
(202) 452-3750

Counsel for defendants.

Plaintiff's Cross-Motion for Summary Judgment in Civil Action No. 80-2614 (D.D.C.)

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2614

A.G. BECKER INCORPORATED,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

PLAINTIFF'S CROSS-MOTION
FOR SUMMARY JUDGMENT

Plaintiff, A.G. Becker Incorporated, ("A.G. Becker"), by its attorneys, Fried, Frank, Harris, Shriver & Kampelman, respectfully moves, pursuant to Rule 56 of the Federal Rules of Civil Procedure, that the Court enter summary judgment in its

favor declaring (1) that the September 26, 1980 final ruling and order (the "Ruling") by the Board of Governors of the Federal Reserve System (the "Board"), holding, as a matter of law, that commercial paper is not a security or a note within the meaning of the Glass-Steagall Act, 48 Stat. 162, and that member banks of the Federal Reserve System are not prohibited by Sections 16 and 21 of the Glass-Steagall Act from dealing in, distributing and underwriting third-party commercial paper, is arbitrary, capricious, an abuse of discretion, without any rational basis, in excess of the Board's statutory authority, and otherwise not in accordance with law and that the Ruling is null and void; (2) that the Board's Ruling refusing to initiate cease-and-desist proceedings against Bankers Trust Company in connection with its third-party commercial paper activities is arbitrary, capricious, an abuse of discretion, without any rational basis, in excess of the Board's statutory authority, and otherwise not in accordance with law and that the Ruling is null and void; and (3) that the Board's actions in connection with A.G. Becker's petition to the Board violated the Government in the Sunshine Act and the Administrative Procedure Act and deprived A.G. Becker of its right to due process of law.

A.G. Becker further respectfully moves for a permanent injunction ordering defendants, their successors, agents and employees, and other representatives to set aside and withdraw the Board's September 26, 1980 Ruling and enjoining them from implementing it or giving it any effect and remanding this action to the Board in order for it to determine whether to initiate cease-and-desist proceedings against Bankers Trust Company and other member banks in connection with their third-party commercial paper activities and further ordering the Board to comply with the Government in the Sunshine Act and the Administrative Procedure Act in connection therewith.

As grounds for this motion, A.G. Becker alleges that it is entitled to such declaratory and injunctive relief as a matter of law on the basis of material facts as to which there is no

genuine issue. The motion is supported by the pleadings, the administrative record before the Board, a Statement of Material Facts as To Which There Is No Genuine Issue, the Affidavit of Thomas R. York and a Memorandum of Points and Authorities In Support of Plaintiff's Cross-Motion for Summary Judgment, all of which are being filed herewith and are incorporated herein by reference.

Respectfully submitted,

/s/ HARVEY L. PITT
Harvey L. Pitt
Henry A. Hubschman
Edson G. Case, Jr.

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& Kampelman
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Attorneys for A.G. Becker
Incorporated

Of Counsel:

Randy A. Harris
General Counsel
A.G. Becker Incorporated
2 First National Plaza
Chicago, Illinois
(312) 630-5000

Dated: February 27, 1981

SIA's Cross-Motion for Summary Judgment in Civil Action No. 80-2730 (D.D.C.)

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2614

A.G. BECKER INCORPORATED,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Plaintiff Securities Industry Association's Cross-Motion for Summary Judgment

Pursuant to Rule 56(b), Federal Rules of Civil Procedure, plaintiff Securities Industry Association hereby moves for summary judgment in its favor, granting the relief as set forth in the annexed proposed Order on the ground that there are no

genuine issues of material fact and plaintiff is entitled to judgment as a matter of law.

In support of its motion, plaintiff respectfully refers the Court to the attached Statement of Material Facts As To Which Plaintiff Contends There Is No Genuine Issue; and to the attached Memorandum of Points and Authorities submitted by Plaintiff Securities Industry Association in Opposition to Defendant's Motion to Dismiss, or Summary Judgment, and in Support of Its Cross-Motion for Summary Judgment.

Respectfully submitted,

/s/ JOHN M. LIFTIN
John M. Liftin
James B. Weidner
Janet R. Zimmer
David A. Schulz
Thomas M. Shoesmith

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(202) 331-7760
Attorneys for the Securities Industry Association

Dated: February 27, 1981

SIA's Statement of Material Facts As to Which There is No Genuine Issue, filed in Civil Action No. 80-2730 (D.D.C.)

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2614

A.G. BECKER INCORPORATED,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,

Plaintiff,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Plaintiff Securities Industry Association's Statement of Material Facts as to Which There is No Genuine Issue

Pursuant to Rule 1-9(h) of this Court, plaintiff Securities Industry Association hereby sets forth, in support of its motion for summary judgment, the following statement of material facts as to which there is no genuine issue in this action:

SIA's Statement of Material Facts

1. During 1978, Bankers Trust Company, New York, New York ("Bankers Trust"), a State-chartered member bank of the Federal Reserve System, began selling commercial paper issued by corporations not related to the bank ("third-party commercial paper"). (R. 6, 9.)*

2. Sometime prior to July 26, 1978, Bankers Trust began distributing to commercial paper issuers sales materials (R. 67-106) in which Bankers Trust offered to expand the distribution of such issuers' commercial paper by acting as a seller of the paper. (R. 67, 69, 73). These sales materials discuss the "advantages of Bankers Trust versus . . . other dealers" (R. 86), including "a specialized sales distribution system that rivals that of dealers" (R. 72) and "a fee that is competitive with that of commercial paper dealers" (R. 87). In addition, Bankers Trust stated that it may, from time to time and without prior commitment, lend the issuer money and take back notes if unable to place all of that issuer's paper, a policy described as allowing Bankers Trust to be "completely competitive." (R. 82).

3. In November 1978, A.G. Becker Incorporated ("Becker") and the Securities Industry Association ("SIA") expressed concern to the staff of the Board of Governors of the Federal Reserve System ("Board") regarding the legality of Bankers Trust's commercial paper activities., (R. 6).

4. In two letters, dated April 20 and June 26, 1979, the Office of General Counsel of the Securities and Exchange Commission advised the Board of its opinion, based on its

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* "R. " refers to the administrative record maintained by the Board with respect to the petitions of A.G. Becker, Inc. and the Securities Industry Association concerning Bankers Trust's commercial paper activities. A copy of this record has been filed with the court.

analysis of the Act and its legislative history, that commercial paper was a "security" within the meaning of the Glass-Steagall Act. (R. 311-320; 329-335.) (Subsequently, by letter dated February 20, 1980 the Securities and Exchange Commission advised the Board that it had reviewed its General Counsel's analysis and concurred in the conclusion that commercial paper is a "security" as that term is used in the Glass-Steagall Act. (R. 559-560.))

5. On June 29, 1979 after a meeting between Board staff and representatives of Becker and the SIA and after numerous written submissions by Becker, the SIA, Bankers Trust, and the General Counsel of the Securities and Exchange Commission (R. 116-279, 283-320, 323-327, 329-335), the Board's General Counsel issued an opinion concluding that commercial banks may, subject to certain limitations, sell third-party commercial paper. (R. 336-361.)

6. By letters to Becker and the SIA dated June 29, 1979, the Board's General Counsel stated that, at the request of either organization, he would recommend that the Board review his opinion. (R. 360-361.)

7. In submissions dated July 26, 1979 and January 31, 1980, respectively, the SIA and Becker requested the Board to review the matter and to initiate formal adjudicatory proceedings to restrain Bankers Trust's activities. (R. 363-414, 554-558.)

8. On September 26, 1980, the Board issued a letter and statement setting forth its conclusion that "commercial paper is not a 'security' within the meaning of the Glass-Steagall Act. The restrictions of the Act against underwriting and dealing in securities thus do not apply to such an instrument." (R. 563.) The Board also expressed its view that "the sale of third party commercial paper by a commercial bank could involve, at least

in some circumstances, potential unsafe or unsound banking practices." (R. 664, 669.)

Dated: February 27, 1981

/s/ JOHN M. LIFTIN
John M. Liftin
James B. Weidner
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Attorneys for the Securities Industry Association

Order of the Federal Energy Regulatory Commission, Docket No. EL81-5-000 (March 17, 1981)

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

ELECTRIC RATES: Interlocking Directorates

Before Commissioners: Georgiana Sheldon, Acting Chairman; Matthew Holden, Jr., George R. Hall and J. David Hughes.

Edison Electric Institute — Docket No. EL81-5-000

ORDER CONCERNING INTERLOCKING DIRECTORATES
(Issued March 27, 1981)

On December 8, 1980, the Edison Electric Institute (EEI) filed a petition calling to the Commission's attention certain questions relating to interlocking directorates raised by recent actions of the Board of Governors of the Federal Reserve System (Board).

Background

Section 305(b) of the Federal Power Act makes it unlawful, in the absence of Commission authorization, for any person to hold the position of an officer or director of a public utility and the position of an officer or director of a bank, trust company, banking association, or firm authorized to underwrite or participate in the marketing of public utility securities. Commercial banks are prohibited by the Glass-Steagall Act from underwriting or marketing securities,[1] and EEI indicates that, in reliance on the prohibitions found in the Glass-Steagall Act, many officers and directors of public utilities now serve as officers or directors of commercial banks without having obtained Commission authorization.

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1 Banking Act of 1933, ch. 89, 48 Stat. 162 (1933); Banking Act of 1935, ch. 614, 49 Stat. 684 (1935).

Order

In July of 1978, the Bankers Trust Company (Trust Company) placed third party commercial paper with certain institutional investors as agent for and on behalf of certain unidentified corporate issuers.[2] The Securities Industry Association (SIA) and A.G. Becker, Inc. (Becker) subsequently requested the Board to review the legality of the Trust Company's actions, alleging *inter alia* that the Trust Company was dealing in securities in violation of the applicable provisions of the Glass-Steagall Act. On September 26, 1980, the Board concluded *inter alia* that commercial paper is not a security within the meaning of the Glass-Steagall Act and that the Trust Company had not violated the applicable provisions of the Glass-Steagall Act.

The SIA and Becker have each filed for review of the Board's finding in the United States Court of Appeals for the District of Columbia Circuit and in the United States District Court for the District of Columbia. The SIA also has filed suit against the Trust Company seeking a declaratory judgment and an injunction in the United States District Court for the Southern District of New York.

As a result of these events, EEI seeks an order of this Commission declaring that it will take no immediate action against individuals serving both as officers or directors of public utilities and officers or directors of commercial banks in response to the Board's determination and that the *status quo ante* will be maintained pending the outcome of the ongoing litigation. EEI believes that any ultimate determination by the Commission should be deferred.

Notice of EEI's petition was issued on January 23, 1981, with responses due on or before February 3, 1981. No responses have been filed.

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2 The commercial paper placed by the Trust Company was not issued by the Trust Company but was issued by corporations not related to the Trust Company; the Trust Company thus is said to have placed third party commercial paper.

Discussion

While commercial banks long have engaged in and continue to engage in the purchase and, less frequently, the sale of commercial paper for their own accounts or for the accounts of their customers,[3] the Trust Company's placement of third party commercial paper departs from commercial banks' traditional role in the commercial paper markets. The Trust Company acted as agent for the issuer, "marketing" commercial paper much like a commercial paper dealer.

The Commission consistently has held that Section 305(b) of the Federal Power Act requires Commission authorization to hold interlocks between public utilities and commercial banks only when commercial banks are authorized by law to underwrite or participate in the marketing of public utility securities.[4] Now, for the first time, commercial banks appear to be "authorized by law to underwrite or participate in the marketing of securities of a public utility" for purposes of section 305(b): the Board's finding appears to authorize commercial banks to "market" third party commercial paper and it appears that, given the broad definition of "security" found in the Federal Power Act,[5] commercial paper is a security for purposes of section 305(b). As a result, the hundreds of public

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3 *Bankers Trust Company*, Findings of the Board of Governors of the Federal Reserve System and Statement Regarding Petitions to Initiate Enforcement Action (September 26, 1980). *See Investment Company Institute* v. *Camp*, 401 U.S. 617 (1971). *See generally* E. Hurley, The Commercial Paper Market, 63 Fed. Res. Bull. 525 (1977).

4 *Arthur F. Davey*, 2 FPC 534 (1939). *See* 55 FPC Ann. Rep. 4 (1975); 54 FPC Ann. Rep. 6 (1974).

5 Section 3(16) of the Federal Power Act provides:

> "security" means any note, stock, treasury stock, bond, debenture, or other evidence of interest in or indebtedness of a corporation subject to the provisions of this Act. 16 U.S.C. § 796(16) (1976).

See also 16 U.S.C. § 824c (1976).

utility officers and directors also serving as commercial bank officers and directors may be in violation of section 305(b). To continue to hold the interlocks, Commission authorization is required.

The abrupt change in the status of those persons now serving as officers or directors of public utilities and officers or directors of commercial banks, coupled with the number of persons affected, persuades the Commission that action is warranted pending the outcome of the ongoing litigation and final Commission resolution. In view of the unique circumstances now before us, we believe it appropriate to authorize the continued holding of such positions on an interim basis, but only if the subject commercial banks have not underwritten or marketed and do not now underwrite or market public utility securities, including commercial paper. It appears that a clear, overriding benefit is to be gained from temporarily authorizing the continued holding of such positions, and that neither public nor private interests will be adversely affected. Moreover, we believe that the sudden change in the status of these individuals and the number involved present good cause to depart from the requirements of Part 45 of our regulations. Accordingly, we shall waive the requirements of Part 45 of our regulations. We shall instead require those persons who seek to take advantage of the interim authorization afforded by our order to file an abbreviated statement identifying the affected interlocks.

Where, however, the subject commercial banks have underwritten or marketed, are now underwriting or marketing, or in the future underwrite or market public utility securities, including commercial paper, those persons holding interlocks must individually seek Commission authorization pursuant to section 305(b) and Part 45 of our regulations. The potential harms sought to be eliminated by the enactment of section 305(b) are most likely to occur when the underwriting or marketing of public utility securities actually takes place;[6] we, therefore, do

6 *See John Edward Aldred*, 2 F.P.C. 247 (1940).

not believe that even interim authorization should be granted in such cases.[7]

Finally, we caution that this interim determination should not be construed as precluding any further action which the Commission may deem warranted as circumstances develop, or as prejudging any substantive questions that subsequently may be presented.

The Commission orders:

(A) Until further order of this Commission, any person now holding or who may hold the positions of officer or director of a public utility and officer or director of a bank subject to the provisions of the Glass-Steagall Act is authorized to hold such positions on an interim basis; *Provided that* the subject bank has not engaged in and does not now engage in, the underwriting or marketing of securities of a public utility, including the commercial paper of a public utility; and *Provided, further,* that such person files the statement required in Paragraph (C) below.

(B) Until further order of this Commission, no person now holding or who may hold the positions of officer or director of a public utility and officer or director of a bank subject to the provisions of the Glass-Steagall Act is authorized to hold such positions if the bank has engaged in, does now engage in, or does in the future engage in the underwriting or marketing of securities of a public utility, including the commercial paper of a public utility, unless that person has obtained authorization to hold such positions pursuant to section 305(b) of the Federal Power Act and Part 45 of the Commission's regulations. 18 C.F.R. Part 45 (1980). Persons now holding such positions and who wish to continue to hold such positions shall file an

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7 Provided that timely applications are filed with respect to this matter, the Commission will not require that the applicants remove themselves from their positions during the pendancy of their applications.

application for authorization under Part 45 of the Commission's regulations within forty-five days.

(C) The requirements of Part 45 of the Commission's regulations are hereby waived with respect to those persons subject to Paragraph (A) above, and those persons, instead, shall file, in conjunction with the statement required by section 305(c) of the Federal Power Act, a statement providing the following information:

(1) full name, business address, and place of residence;

(2) public utilities with which the person holds the positions of officer or director, and identifying those positions;

(3) banks subject to the provisions of the Glass-Steagall Act with which the person holds the positions of officer or director, and identifying those positions.

(D) This order shall not affect the liability of any person under section 305(a) of the Federal Power Act or under any other provision of that Act.

(E) The Secretary shall promptly publish this order in the Federal Register.

By the Commission.

(SEAL)

/s/ KENNETH F. PLUMB
Kenneth F. Plumb,
Secretary.

Order of the Federal Energy Regulatory Commission, Docket No. EL81-5-000 (May 26, 1981)

15 FERC ¶ 61-173

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Electric Rates: Rehearing; Intervention; Interlocking Directorates

Before Commissioners: Georgiana Sheldon, Acting Chairman; Matthew Holden, Jr., and J. David Hughes.

Edison Electric Institute — Docket No. EL81-5-000

ORDER GRANTING INTERVENTION, GRANTING REHEARING FOR PURPOSE OF RECEIVING FURTHER COMMENTS, AND CLARIFYING PRIOR ORDER
(Issued May 26, 1981)

By order issued March 27, 1981, the Commission determined that persons serving as officers or directors of public utilities and officers or directors of commercial banks were authorized to hold such positions upon a minimal filing provided that the subject banks did not engage in the underwriting or marketing of public utility securities, including commercial paper. If, however, the subject banks engaged in underwriting or marketing public utility securities, including commercial paper, such persons were required to seek individual authorization pursuant to Part 45 of the Commission's regulations. 18 C.F.R. Part 45 (1980).

On April 10, 1981, the Continental Illinois National Bank and Trust Company of Chicago (CINB) petitioned to intervene out of time. On April 24, 1981, CINB filed an application for rehearing. CINB states that it is a commercial bank with two directors who also serve as directors of public utilities and that it has numerous relationships with public utilities subject to the

Commission's jurisdiction. CINB argues that it did not receive adequate notice of this proceeding and so it did not previously petition to intervene. The comments and analysis of CINB and of the commercial banking industry, CINB submits, would have been and will be of great benefit to the Commission in this proceeding. Moreover, CINB argues that the Commission improperly determined that commercial banks are authorized to underwrite or market public utility securities and that the Commission's authority thus extends to interlocks between public utilities and commercial banks. Finally, CINB argues that the holding of such interlocks does not adversely affect public or private interests. CINB asks in the alternative that the Commission (1) reverse its order of March 27, 1981 and find that commercial banks are not authorized to underwrite or market public utility securities; (2) vacate its order of March 27, 1981 and permit all interested parties to address the merits of the questions before the Commission; or (3) stay its order of March 27, 1981 until the actions now ongoing in the courts are resolved.

We find that CINB's participation in this proceeding is in the public interest and that good cause exists to grant the untimely petition. Accordingly, we shall grant CINB's petition to intervene out of time. In this instance, we also believe that further input from interested persons should be permitted. CINB has requested an opportunity to comment further on the structure of the commercial banking industry and how it would be affected by our order of March 27, 1981 in this proceeding. *Because the commercial banking industry is one with which the Commission does not ordinarily have direct involvement*, we believe that it is appropriate to grant CINB's request to comment further and to afford an additional opportunity for comment to all interested persons. Accordingly, we shall invite interested persons, whether or not parties, to file responses to the application for rehearing or additional comments on our prior order in the form of briefs, to be submitted within forty-five days of the issuance of this order.

Order

We shall further amend our prior order to resolve the ambiguities that may have resulted and to clarify the Commission's intent, particularly with regard to the filing requirement found in ordering paragraph (C) of that order. These clarifications also respond to allegations of a technical violation of the Paperwork Reduction Act of 1980.

The Commission orders:

(A) The petition to intervene is hereby granted subject to the rules and regulations of the Commission; *provided, however,* that participation by the intervenor shall be limited to matters set forth in its petition to intervene; and *provided, further,* that the admission of the intervenor shall not be construed as recognition by the Commission that it might be aggrieved because of any order or orders by the Commission entered in this proceeding.

(B) The application for rehearing is hereby granted for purposes of further hearing. Responses to the application for rehearing and additional comments on the order issued March 27, 1981 in this proceeding are invited from any interested persons, whether or not parties, within 45 days of the issuance of this order.

(C) Ordering paragraphs (A), (B), and (C) of the Commission's order issued March 27, 1981 in the instant docket are hereby amended to read as follows:

> (A) Until further order of this Commission, any person holding the positions of officer or director of a public utility and officer or director of a bank subject to the provisions of the Glass-Steagall Act is authorized to hold such positions on an interim basis; *provided* that the subject bank does not engage in the underwriting or participate in the marketing of securities of a public utility, including commercial paper; and *provided, further,* that such person files the statement required in Paragraph (C) below.

(B) Until further order of this Commission, no person holding the positions of officer or director of a public utility and officer or director of a bank subject to the provisions of the Glass-Steagall Act is authorized to hold such positions if the subject bank engages in the underwriting or participates in the marketing of securities of a public utility, including commercial paper, unless that person has obtained authorization to hold such positions pursuant to section 305(b) of the Federal Power Act and Part 45 of the Commission's regulations. Those persons who wish to continue to hold such positions shall file an application for authorization pursuant to Part 45 of the Commission's regulations within either forty-five days of the date the subject bank engages in the underwriting or participates in the marketing of securities of a public utility, including commercial paper, or within 45 days of the date of issuance of this order, whichever is later.

(C) Until further order of this Commission, the full requirements of Part 45 of the Commission's regulations, except as required below, are hereby waived with respect to those persons subject to Paragraph (A) above. In lieu of the full requirements of Part 45 of the Commission's regulations, those persons shall file an application providing only the following information:

(1) full name and business address;

(2) all public utilities with which the person holds the positions of officer or director, and identifying those positions;

(3) all banks subject to the provisions of the Glass-Steagall Act with which the person holds the positions of officer or director and identifying those positions.

(C) The Secretary shall promptly publish this order in the Federal Register.

By the Commission.

(SEAL)

/s/ KENNETH F. PLUMB
Kenneth F. Plumb,
Secretary.

Board Press Release, dated May 28, 1981

FEDERAL RESERVE PRESS RELEASE

May 28, 1981

For immediate release

The Federal Reserve Board has adopted a policy statement providing guidelines to govern the sale by State member banks of commercial paper issued by firms not related to the bank.

The Board's guidelines concerning the sale of such third party commercial paper (promissory notes of corporations) are intended to assure safe and sound banking practices. The Board said it would monitor activity in this area closely and would modify or supplement its guidelines as indicated by experience.

The policy statement is effective immediately. However, the Board will accept comment, for review by the Board, through July 31, 1981.

The policy statement calls for:

—Limitation of sales to prime quality commercial paper meeting specifications in the statement.

—Careful analysis and monitoring by the seller of the creditworthiness of the issuer.

—Adoption by the selling bank of rules limiting the amount of commercial paper that may be sold for single or related issuers.

—Extensive record keeping and maintenance of records.

—No sales to fiduciary accounts over which the bank has investment discretion, or to the bank's parent bankholding company (unless it is a bank) or to a nonbank affiliate of the bank.

—Certain notices to buyers.

These guidelines are spelled out in the attached statement.

Attachment

Federal Reserve System, *Policy Statement Concerning the Sale of Third-Party Commercial Paper by State Member Banks*, dated May 26, 1981

POLICY STATEMENT CONCERNING THE SALE OF THIRD PARTY COMMERCIAL PAPER BY STATE MEMBER BANKS

[Docket No. R-0360]

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Policy Statement

SUMMARY: Pursuant to its authority to restrain unsafe or unsound banking practices by State member banks, the Board of Governors of the Federal Reserve System adopts a policy statement setting forth guidelines governing the sale by a State member bank of commercial paper of issuers not related to the bank ("third party commercial paper"). The guidelines reflect the Board's judgment that certain practices may develop in the sale by a bank of third party commercial paper that may not be consistent with the principles of safe and sound banking. The guidelines concern the type and amount of commercial paper that should be sold, the kinds of records that should be maintained, and the purchasers to which such paper may be sold. The Board intends to monitor closely the activities of State member banks in this area and may modify or supplement this policy statement based on the Board's review of the experience of State member banks in conducting these activities.

EFFECTIVE DATE: May 26, 1981. Interested parties may submit comments on the policy statement that will be reviewed by the Board. Comments must be received on or before July 31, 1981.

ADDRESS: Comments should include reference to Docket No. R-0360 and should be mailed to the Secretary, Board of Governors of the Federal Reserve System, 20th and Constitution Avenue, N.W., Washington, D.C. 20551, or delivered to Room B-2223, 20th and Constitution Avenue, N.W., Washing-

ton, D.C. between 8:45 a.m. and 5:15 p.m. Comments may be inspected in Room B-1122 between 8:45 a.m. and 5:15 p.m.

FOR FURTHER INFORMATION CONTACT: Robert S. Plotkin, Assistant Director, Division of Banking Supervision and Regulation, (202) 452-2782, or Richard Ashton, Senior Counsel, Legal Division, (202) 452-3750, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.

SUPPLEMENTAL INFORMATION: On September 26, 1980, the Board took action with respect to the petitions of the Securities Industry Association (the "SIA") and of A.G. Becker Incorporated ("A.G. Becker") that the Board prohibit Bankers Trust Company, New York, New York ("Bankers Trust"), a State member bank, from selling third party commercial paper. The Board denied the petitions to the extent they alleged that Bankers Trust's commercial paper activities violate the Glass-Steagall Act or should be prohibited by general considerations of public policy. The Board also stated that the sale of third party commercial paper by a commercial bank could involve, at least in some circumstances, potential unsafe or unsound practices. The Board thus took no action on the petitions' allegations of dangers to Bankers Trust or potential conflicts of interest pending development of general supervisory guidelines designed to avoid potential unsafe or unsound practices in the sale of third party commercial paper by State member banks.

In developing the guidelines that are set forth in the following policy statement, the Board has consulted with the staffs of the other federal banking agencies and has considered the allegations of unsafe practices made by the SIA and A.G. Becker and the comments of the Securities and Exchange Commission.

With respect to the possibility that a bank's commercial paper selling activities may lead the bank into investing its funds in imprudent investments, the Board recognizes that a bank's selling activity may result in the purchase of some commercial paper with the bank's own funds. However, the Board notes that banks have traditionally been permitted to purchase commercial paper for their own account and such

purchases have been treated for supervisory purposes as commercial loans. In addition, since only large, well-known corporations with established credit ratings are able to market unsecured obligations, commercial paper is generally a low-risk instrument, even relative to some commercial loans.[1] Furthermore, the Board's guidelines provide that a bank should sell only prime quality paper and make a thorough credit analysis of each issuer and that all commercial paper sold by the bank should be fully supported by available lines of credit.[2] These guidelines would also minimize the danger that a bank selling commercial paper might be tempted to make unsound loans to an issuer which is encountering financial difficulties in order to protect the bank's reputation.

The SIA, A.G. Becker, and the SEC have also raised the possibility of loans by a selling bank to facilitate purchase of commercial paper being sold by the bank. However, because rates on commercial paper are usually lower than rates charged on bank loans, the use of borrowed funds to purchase commercial paper would be unprofitable and thus unlikely. Accordingly, there does not appear to be any practical substance to this concern.

Another potential hazard cited in connection with bank sales of commercial paper is the possibility that the bank's salesman's interest might impair its existing obligations to its customers and might consequently damage the bank's good will and reputation. In particular, it is claimed that bank depositors might suffer losses on paper purchased from the bank, that "the bank's reputation for prudence and restraint would be abused," that the bank would lose its ability to provide disinterested investment advice, and that the bank

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1 The Board notes that, at least on some occasions, significant losses have been suffered by commercial paper purchasers, for example, the 1970 collapse of Penn Central Transportation Company. However, banking functions, such as commercial lending, also involve some degree of risk and losses can and do occur.

2 A selling bank could only participate in the line of credit up to the amount of its legal lending limit.

might "unload" worthless commercial paper in its trust department.

Under the Board's guidelines, however, a bank may sell commercial paper only to financially sophisticated purchasers and may not advertise commercial paper for sale to the general public. Thus, there appears to be little likelihood that any but a small fraction of a bank's depositors would even consider purchasing commercial paper being sold by the bank. For the same reason, the potential for a bank abusing its reputation for "prudence and restraint" in selling commercial paper does not appear significant. Finally, with respect to potential inability to provide disinterested investment advice and "unloading" of worthless commercial paper in the bank's trust accounts, the guidelines provide that the bank should not sell commercial paper to fiduciary accounts over which the bank has investment discretion.

The Board intends to monitor closely the selling activities of Bankers Trust and any other State member bank that may initiate such services. Based on further experience in this area, the Board may modify or supplement these guidelines to assure that such activities are conducted in accordance with principles of safe and sound banking.

Accordingly, acting pursuant to its supervisory authority over State member banks contained in section 9 (12 U.S.C. 321, *et seq.*) and section 11 (12 U.S.C. 248) of the Federal Reserve Act and the Financial Institutions Supervisory Act of 1966 (12 U.S.C. 1818(b)) and related provisions of law, the Board of Governors adopts the following policy statement.

Policy Statement Concerning Sale of Third Party Commercial Paper by State Member Banks

The Board of Governors has recently determined that the sale of commercial paper by a State member bank for unaffiliated issuers ("third party commercial paper")[3] did not violate

[3] Excluding commercial paper issued by a parent bank holding company; the Board has previously advised bank holding companies concerning sales of bank holding company commercial paper (letter dated June 27, 1980).

the Glass-Steagall Act (12 U.S.C. §§ 24, Seventh, 378). The Board was concerned however, that the sale of third party commercial paper[4] might, in some circumstances, involve unsafe or unsound practices. Accordingly, in the interest of safe and sound banking, the Board believes that any State member bank that may decide to engage in the sale of third party commercial paper should adhere to the following guidelines.[5]

1. A State member bank should sell only prime quality commercial paper that qualifies for the exemption provided by section 3(a)(3) of the Securities Act of 1933 (15 U.S.C. 77c(a)(3)). The bank should take appropriate precaution to assure itself that the section 3(a)(3) exemption applies to the commercial paper it proposes to sell. In this regard, (i) the bank should determine that the commercial paper it proposes to sell is of prime quality; (ii) the bank may rely on representations of the issuer with respect to the use of proceeds; (iii) except as further limited by paragraphs 7 and 8, the bank should sell commercial paper only to financially sophisticated customers, such as customers that regularly purchase a variety of short-term credit instruments, and should not advertise commercial paper for sale to the general public; (iv) the bank should obtain periodically, and maintain in the bank's records, a current legal opinion of counsel that the section 3(a)(3) exemption is available. In addition, the bank should sell commercial paper in minimum denominations that are consistent with applicable law and, in no event, should sell commercial paper in minimum denominations of less than $100,000

2. The selling bank should maintain a complete credit analysis of the issuer at all times and should exercise due diligence

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4 Banks have traditionally purchased commercial paper upon the order, and for the account of, customers, whereas here the bank is essentially acting for the issuer; the former activity is not subject to the guidelines set forth in this Policy Statement.

5 The Board does not expect to take enforcement action to restrain unsafe or unsound banking practices with respect to third-party commercial paper selling activities of any State member bank that conducts such activities within these guidelines.

in investigating the financial affairs of the issuer. Particular attention should be given to the liquidity position of the issuer and its lines of credit. All commercial paper sold by the bank should be fully supported by available lines of credit. Any participation by the selling bank in such lines of credit should be made only after consideration of the bank's legal lending limit.

3. Senior management should adopt internal limits for the amount(s) of commercial paper that may be sold by the bank for a single or related issuer(s). In determining the internal limits, senior management should consider the financial condition of the issuer, all lines of credit available to the issuer, and the bank's participation in the lines of credit and any other extensions of credit or commitments to the issuer by the bank (including commercial paper purchased by the bank for its own account.)

4. Chronological records of original entry should be maintained that contain an itemized daily record of all sales and purchases of commercial paper. The records should also contain:

- A designation of the commercial paper,
- nature of the transaction, *e.g.* purchase or sale,
- trade and settlement dates,
- contra-party name or designation,
- net proceeds, discount rate, or yield to maturity.

5. Account records should be maintained for each issuer that reflect:

- All sales and purchases of commercial paper placed by the bank for that issuer,
- all lines of credit available to the issuer,
- the amount of the bank's participation in the lines of credit,
- a current balance of all extensions of credit and a description of other commitments to the issuer.

Policy Statement

6. Account records should be maintained for each purchaser that reflect all sales and purchases of commercial paper for the account of that customer.

7. Commercial paper should not be sold to fiduciary accounts over which the bank has investment discretion.

8. Commercial paper should not be sold to the bank's parent holding company (unless it is a bank) or any nonbank affiliate of the bank.

9. The bank should furnish to all purchasers of commercial paper written advice in connection with all purchases that (1) the commercial paper is not an obligation of the bank, and is not insured by the FDIC, (2) the bank has no obligation to repurchase any of the paper sold, (3) the bank is under no obligation to lend funds to the issuer (except pursuant to existing credit lines, or other commitments, if any), and (4) copies of the issuer's most recently published financial statements will be furnished upon request.

By order of the Board of Governors, May 26, 1981.

(signed) James McAfee

James McAfee
Assistant Secretary of the Board

(SEAL)

Excerpts from Transcript of Oral Argument in Civil Action No. 80-2730 (D.D.C.) on July 18, 1981 before Hon. Joyce Hens Green [pages 1-2, 16-17]

IN THE
UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 80-2614

A. G. BECKER, INC.,

Plaintiffs,

vs.

THE BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Civil Action No. 80-2730

SECURITIES INDUSTRY ASSOCIATION,

Plaintiffs,

vs.

THE BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

Washington, D.C.
Thursday, June 18, 1981

The above-entitled matter came on for hearing before the Honorable JOYCE HENS GREEN, United States District Judge, commencing at approximately 10:00 a.m.

Transcript of Oral Argument

APPEARANCES:

On behalf of A. G. Becker, Inc.:

HARVEY L. PITT, Esquire
HENRY A. HUBSCHMAN, Esquire
EDSON G. CASE, Esquire

PROCEEDINGS

THE DEPUTY CLERK: Civil Action 80-2614, A.G. Becker, Inc. versus the Board of Governors of the Federal Reserve System, et al., and Civil Action 80-2730, the Securities Industry Association versus the Board of Governors of the Federal Reserve System, et al.

MR. ASHTON: Good morning, Your Honor.

THE COURT: Good morning.

MR. ASHTON: May it please the Court.

My name is Richard Ashton, and I'm an attorney with the Federal Reserve Board. I will be presenting all argument this morning on behalf of the Board in support of its motions to dismiss, or in the alternative, for summary judgment in these cases, A. G. Becker versus the Board of Governors and the Securities Industry Association versus the Board of Governors.

THE COURT: Would you like to introduce the people who are at counsel table with you.

MR. ASHTON: Yes, I would.

Sitting at the counsel table with me are J. Virgil Mattingly, Jr., Associate General Counsel, and Melanie L. Fein, who is an attorney on the staff of the Federal Reserve Board also.

The arguments in this case have been exhaustively briefed in the numerous papers filed in this case. I would

[material deleted]

regularly as part of their business. As the Board found, the record indicates that the transaction represented by Bankers Trust, the commercial paper sold by Bankers Trust meets these criteria. It's undisputed that the paper is short term.

The record indicates that the average maturity of this paper is around 60 days. It's also clear that there are relatively few lenders, and no more than 15 in the case of any one particular issue, and Bankers Trust sells commercial paper in very large denominations, large enough so that an average investor would be unable to purchase them. The record indicates that the average denomination on the commercial paper Bankers Trust sells, is around a million dollars, minimum denomination.

And finally, the record indicates that the purchasers of the commercial paper from Bankers Trust are part of the bank's established base of institutional purchasers, who regularly purchase short term credit obligations, and thus are regularly extending credit. They are the functional equivalent of lenders.

Put another way: The Board found that Bankers Trust activity in selling the commercial paper is functionally the same as a bank's activities in selling loan notes in connection with a loan participation.

It's crucial to note that the Board's analysis here depends on the combination of all the particular facts involved. The Board did not say that any one particular fact was determinative. The Board didn't say that all short term notes were not securities, it didn't say that all nonspeculative notes were not securities. The Board's determination is based on this particular combination of the factors involved. If the factors change, for example, if Bankers Trust began selling commerical paper in very small denominations or marketing it to the public, then the Board's conclusion is very likely to change.

The plaintiffs have tried to attack this functional finding by the Board by alleging that since Bankers Trust activity involves a marketing activity, it must be a security, but as we demonstrated, of course, the extent to which marketing is involved, is to some extent relevant. If the commercial paper were marketed widely, it might be a security, but the marketing activity here is limited, it's limited to an narrow class of customers, customers that are functionally equivalent to lenders.

And finally, the Glass-Steagall Act does not prohibit banks from engaging in marketing activities. It prohibits them from underwriting marketing securities. The Board's finding that commercial paper is not a security for purposes of the Glass-Steagall Act, is bolstered by its finding that commercial paper does not meet the statutory definition of investment security in Section 16.

Opinion of the United States District Court

UNITED STATES DISTRICT COURT
DISTRICT OF COLUMBIA

Civ. A. Nos. 80-2614, 80-2730

July 28, 1981

A.G. BECKER INCORPORATED,

Plaintiff,

v.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

SECURITIES INDUSTRY ASSOCIATION,

Plaintiff,

v.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Defendants.

APPEARANCES:

Harvey L. Pitt, Henry A. Hubschman, Edson G. Case, Jr., Fried, Frank, Harris, Shriver & Kampleman, Washington, D.C., for Becker.

John M. Liftin, James B. Weidner, Janet R. Zimmer, Rogers & Wells, Washington, D.C., for SIA.

Richard M. Ashton, Neal L. Petersen, James V. Mattingly, Jr., Federal Reserve Board, Washington, D.C., for defendants.

JOYCE HENS GREEN, *District Judge.*

Pending before the Court in these consolidated actions are the parties' cross motions for summary judgment and the defendant's alternative motion to dismiss, with supporting memoranda. Plaintiffs are A.G. Becker, Inc. ("Becker"), a securities broker and dealer registered with the Securities and Exchange Commission, and the Securities Industry Association ("SIA"), an organization representing over five hundred securities brokers and dealers. They challenge a decision of the Board of Governors of the Federal Reserve System ("the Board"), which, with its individual members, are the defendants in this action. The dispute presents provocative questions concerning the delicately balanced regulatory system enacted by Congress to control the activities of the nation's banks in financial markets.

In the summer of 1978, Bankers Trust Company ("Bankers Trust"), a state chartered member bank of the Federal Reserve System, began offering for sale third party commercial paper, that is, commercial paper issued by corporations not related to the bank.[1] This effort included a marketing campaign aimed at

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1 A succinct definition of commercial paper is offered in Comment, *The Commercial Paper Market and the Securities Acts*, 39 U.Chi. L. Rev. 362 (1972):

> Commercial paper consists of unsecured, short-term promissory notes issued by sales and personal finance companies; by manufacturing, transportation, trade, and utility companies; and by the affiliates and subsidiaries of commercial banks. The notes are payable to the bearer on a stated maturity date. Maturities range from one day to nine months, but most paper carries an original maturity between thirty and ninety days. When the paper becomes

issuers of commercial paper, whereby Bankers Trust agreed to act as a seller of commercial paper, performing services competitive with securities dealers. As part of this advertising, Bankers Trust offered to lend the issuer of commercial paper money equal to the amount of paper to be sold and, if the bank were unable to sell all of the issuer's paper, to take back notes reflecting the amount of paper unsold.

Becker and SIA expressed concern to the staff of the Board of Governors as to the legality of Bankers Trust's actions in a letter sent in November, 1978. Following this correspondence, plaintiffs, along with the General Counsel of the Securities and Exchange Commission ("SEC") and Bankers Trust, filed memoranda arguing over whether the sale by Bankers Trust of third party commercial paper violated certain provisions of the Banking Act of 1933 known as the Glass-Steagall Act. On June 28, 1979, after a meeting with representatives of Becker and SIA, the General Counsel of the Board issued a document entitled "Commercial Paper Activities of Commercial Banks: A Legal Analysis," which concluded that state member banks may, subject to certain limitations, sell third party commercial paper. The General Counsel offered, upon request by Becker or SIA, to recommend that the Board review his opinion. SIA, on July 26, 1979, and Becker, on January 31, 1980, requested that the Board review the General Counsel's opinion and that, in connection with that review, they initiate proceedings against Bankers Trust for violating the Glass-Steagall Act.[2]

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due, it is generally rolled over—that is, reissued—to the same or a different investor at the market rate at the time of maturity.

Id. at 363-64 (footnotes omitted).

2 Because it may affect the jurisdiction over this action, the parties dispute vigorously whether plaintiffs requested that the Board initiate cease and desist proceedings. Suffice it to quote from plaintiffs' precise language:

> This application is intended to . . . renew the SIA's request for formal action by the Board requiring Bankers Trust Company to cease and desist from its illegal activities. (Application of SIA for Review of State Member Bank Action, July 26, 1979 at 3; Record at

The Board took up the matter presented by the Becker and SIA petitions and, on September 26, 1980, issued a letter and a Statement Regarding Petitions to Initiate Enforcement Actions declaring that commercial paper was not a security within the meaning of the Glass-Steagall Act and that therefore Bankers Trust could legally sell third party commercial paper. The Board expressed concern at some potentially unsound practices that might have developed as a result of its ruling, and therefore commenced the drafting of guidelines governing the sale by state member banks of commercial paper.[3] Soon thereafter, the plaintiffs commenced this action seeking judicial review of the Board's conclusion that Bankers Trust was acting

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366) (Citations to the administrative record will be made as "R. at __").

. . . Applicant SIA respectfully asserts that the Board should (1) formally review this matter, (2) Order Bankers Trust to cease and desist from its third party commercial paper activity . . . *Id.* at 20, R. at 383.

. . . this memorandum is submitted to urge the Board . . . to advise Bankers Trust that its current commercial paper marketing activities are inappropriate as a matter of law and policy, and should cease. (Memorandum on Behalf of A. G. Becker Incorporated to the Staff of the Board of Governors of the Federal Reserve System Concerning the Commercial Paper Activities of Bankers Trust Company, January 31, 1980 at 3, R. at 154) The advance of Bankers Trust into the commercial paper market exceeds the boundary of any fair interpretation of where Congress intended the line to be drawn. We respectfully urge the Board, in conformity with the provisions of the Glass-Steagall Act, to issue a declaration to that effect. *Id.* at 47, R. at 198.

The petition submitted by Becker on January 31, 1979, was referred to in their letter exactly one year later seeking review of the General Counsel's opinion.

3 These guidelines were issued in the context of a policy statement on May 28, 1981, effective immediately, to govern the sale of third party commercial paper by state member banks. The Board indicated that it would accept comments on the guidelines through July 31, 1981, and that it will monitor the activities of banks in the commercial paper market to permit modification or supplementation of the guidelines as experience suggests may be fruitful. Plaintiffs' challenge to the Board's action does not include an attack on these guidelines.

within the parameters of the Glass-Steagall Act in offering for sale third party commercial paper.[4]

Surfacing intially in this controversy is the question whether this court, or any court, has jurisdiction to hear this dispute and grant plaintiffs their requested relief. It is beyond dispute that agency action is reviewable absent a showing that Congress specifically and clearly intended to preclude judicial oversight. The Board in this case has the burden of demonstrating that its decision to permit state member banks to sell third party commercial paper is insulated from review. *See Dunlop* v. *Bachowski*, 421 U.S. 560, 567, 95 S. Ct. 1851, 1857, 44 L. Ed. 2d 377 (1975); *Barlow* v. *Collins*, 397 U.S. 159, 166, 90 S. Ct. 832, 837, 25 L. Ed. 2d 192 (1970); *Abbott Laboratories* v. *Gardner*, 387 U.S. 136, 140 n.2, 87 S. Ct. 1507, 1511, 18 L. Ed. 2d 681 (1967). In *Independent Bankers Association of America* v. *Board of Governors of the Federal Reserve System*, 500 F.2d 812 (D.C. Cir. 1974), the Court of Appeals declared that "non-reviewability must be established by a clear showing

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4 Prior to the filing of this action challenging the substance of the Board's ruling, Becker sought relief in this Court for alleged violations by the Board of the Government in the Sunshine Act, 5 U.S.C. § 552b. On November 26, 1980, this Court issued a memorandum opinion containing a declaratory judgment that the defendants violated the Act's premeeting notice requirements but finding that in all other respects, the Board had acted lawfully. That decision, *A. G. Becker Inc.* v. *Board of Governors of the Federal Reserve System*, 502 F. Supp. 378 (D.D.C. 1980), *appeal docketed*, May 4, 1981, will be referred to as *Becker* I.

Additionally, Becker filed, concurrently with this action, a petition in the Court of Appeals for the District of Columbia Circuit, *A. G. Becker, Inc.* v. *Board of Govenors of the Federal Reserve System*, No. 80-2258 (D.C. Cir., filed Oct. 14, 1980), seeking review of the Board's determination that the sale by state member banks of third party commercial paper did not violate the Glass-Steagall Act. The actions were filed in both courts pursuant to the suggestion in the Court of Appeals that "[i]f any doubt as to the proper forum exists, careful counsel should file suit in both the court of appeals and the district court . . . ." *Investment Company Institute* v. *Board of Governors*, 551 F.2d 1270, 1280 (D.C. Cir. 1977). Becker's motion to stay its action in the Court of Appeals is pending.

of Congressional intent to preclude review." *Id.* at 814. Especially where an agency has resolved a pure question of law, which the Board did when it decided that commercial paper was not subject to the proscriptions of the Glass-Steagall Act,[5] courts have a special competence and judicial review is clearly the norm. *See Natural Resources Defense Council, Inc.* v. *Securities and Exchange Commission*, 606 F.2d 1031, 1048 (D.C. Cir. 1979).

The Board contends that the availability of judicial review is governed by the Financial Institutions Supervisory Act of 1966, as amended, which established procedures for the issuance of cease and desist orders by federal agencies with authority over the banking industry. Alternatively, it maintains that its refusal to commence enforcement proceedings against Bankers Trust is a matter committed to its discretion by law and therefore nonreviewable under the Administrative Procedure Act. The plaintiffs strenuously reject that Congess has entrusted the Board with absolute discretion over this matter, suggesting that the Board's interpretation of the Glass-Steagall Act is subject to the normal presumption favoring judicial review absent a showing by the Board of clear deprivation of the Court's jurisdiction. Neither ground for nonreviewability cited by the Board, plaintiffs contend, overcomes the doctrine that permits courts to review agency decision on questions of law.

The Board's initial authority for its argument that jurisdiction lacks is the Financial Institutions Supervisory Act of 1966, as amended, specifically 12 U.S.C. §§ 1818(h), (i). This legislation established procedures for the Federal Deposit Insurance Corporation, the Comptroller of the Currency, and the Board to regulate the nations financial houses and to enforce against

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5 Even the Board recognized that its conclusions necessitated a resolution of a legal question. *See* Letter to plaintiffs' counsel, September 28, 1980 at 3, R. at 664 (". . . the issues involved in these petitions are primarily legal in nature . . . "); Statement Regarding Petitions to Initiate Enforcement Actions, September 28, 1980, at 28, R. at 692 (". . . the Glass-Steagall Act issues resolved by the Board are essentially legal in nature . . . ").

unsafe or unsound banking practices. It provides, in pertinent part:

> (h)(2) . . . any person required by an order issued under this section to cease and desist from any of the violations or practices stated therein, may obtain a review of any order . . . by the filing in the court of appeals of the United States for the circuit in which the home office of the bank is located, or in the United States Court of Appeals for the District of Columbia Circuit . . . a written petition praying that the order of the agency be modified, terminated, or set aside . . . .
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> . . .
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> (i)(1) The appropriate Federal banking agency may in its discretion apply to the United States district court . . . within the jurisdiction of which the home office of the bank is located, for the enforcement of any effective and outstanding notice or order issued under this section, and such courts shall have jurisdiction and power to order and require compliance herewith; but except as otherwise provided in this section no court shall have jurisdiction to affect by injunction or otherwise the issuance or enforcement of any notice or order under this section, or to review, modify, suspend, terminate, or set aside any such notice or order.

Under the Board's view, its decision not to institute cease and desist proceedings and its judgment that commercial paper is not a security under the Glass-Steagall Act are insulated from judicial scrutiny by these provisions. A decision not to adjudicate whether Bankers Trust's conduct was illegal is, in the Board's opinion, analogous to decisions by the Federal Trade Commission and the General Counsel of the National Labor Relations Board exercising their "prosecutorial discretion." *See Moog Industries, Inc.* v. *Federal Trade Commission*, 355 U.S. 411, 78 S. Ct. 377, 2 L. Ed. 2d 370 (1958); *Federal Trade Commission* v. *Klesner*, 280 U.S. 19, 46 S. Ct. 102, 70 L. Ed. 404 (1929) (both holding unreviewable a decision by the Federal Trade Commission not to institute cease and desist pro-

ceedings under section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45) and *National Labor Relations Board* v. *Sears, Roebuck & Co.*, 421 U.S. 132, 138, 95 S. Ct. 1504, 1510, 44 L. Ed. 2d 29 (1975); *Vaca* v. *Sipes*, 386 U.S. 171, 182, 87 S. Ct. 903, 912, 17 L.Ed. 2d 842 (1967) (holding unreviewable a decision of the General Counsel of the Board not to issue an unfair labor practice complaint). The Board also finds shelter for this position in the language of the statute quoted above, in that an injunction directing the Board begin a proceeding to prevent Bankers Trust to sell third party commercial paper would, of necessity, "affect" the issuance of a cease and desist order and thus contravene 12 U.S.C. § 1818(i)(1).

The Board, however, ignores the procedural posture of the proceedings before it and before this Court. 12 U.S.C. § 1818(i) is a narrow statute, applying only to an "order issued under this section." Section 1818 establishes a detailed procedure to govern efforts by the Board to enforce against unsafe and unsound practices. None of these procedures were followed in this case. The Act provides for proper notice, a hearing, service of the Board's findings upon the bank under investigation, and review of the Board's decision in a court of appeals. In this action, Becker and SIA submitted materials to the General Counsel, who issued a legal opinion on the meaning of the Glass-Steagall Act as applied to Bankers Trust's conduct. The General Counsel, while soliciting materials from Bankers Trust, held no formal hearing but rather worked with his staff to reach a resolution of plaintiffs' expressed concerns. He gave the plaintiffs the oportunity to request that he seek review of his own decision by the Board of Governors. Plaintiffs then sought from the Board of Governors a review of the General Counsel's legal opinion and, in connection with that review, the institution of enforcement proceedings. The Board agreed with its General Counsel and decided not to institute an adjudication against Bankers Trust. At this stage, where the plaintiffs are challenging the legal conclusion reached by the General Counsel and adopted by the Board, § 1818 does not proscribe review.

This analysis finds support in *Groos National Bank* v. *Comptroller of the Currency*, 573 F.2d 889 (5th Cir. 1978). The appellate court held that jurisdiction did not vest in the district court to issue a declaratory judgment against the Comptroller, but explicitly found that "the Comptroller [had] set in motion cease and desist proceedings as authorized by 12 U.S.C. § 1818." *Id.* at 892. This is not an action such as *Groos* where "this regulatory process is not to be disturbed by untimely judicial intervention," *id.* at 895, because the administrative process here has reached a final conclusion that the Glass-Steagall Act is not violated when a state member bank sells commercial paper issued by unrelated corporations.

Moreover, it is a well recognized exception to statutes precluding judicial review that if an agency acts beyond the scope of its statutory authority, courts may exercise jurisdiction to overturn that administrative action. *See Manges* v. *Camp*, 474 F.2d 97 (5th Cir. 1973) (decision of Comptroller of the Currency outside of its authority is reviewable notwithstanding § 1818). *See also Leedom* v. *Kyne*, 358 U.S. 184, 79 S. Ct. 180, 3 L. Ed. 2d 210 (1958) (action within discretion of National Labor Relations Board General Counsel is reviewable if he exceeds statutory authority).

Section 1818 does, however, preclude the Court from granting plaintiffs' prayer that an injunction be issued ordering that cease and desist proceedings be commenced against Bankers Trust. *See* Becker Complaint at 11, ¶ 6; SIA Complaint at 8, ¶ 5. It is beyond the jurisdiction of this court, and probably any court, to order the Board, by injunction, writ of mandamus, or otherwise, to begin cease and desist proceedings against a bank. Such a directive would surely intrude upon the limitation set out in § 1818(i)(1), that "no court shall have jurisdiction to affect by injunction or otherwise the issuance . . . of any notice or order under this section . . . ." It is clear, therefore, that the Court's power to grant relief in this action is limited to reviewing the legal conclusion reached by the Board concerning the meaning of the Glass-Steagall Act, and to issuing whatever declaratory order may be appropriate.

As a second and independent ground for its argument that the Court lacks jurisdiction, the Board maintains that its decision that Bankers Trust is not violating the Glass-Steagall Act is wholly within its discretion and therefore unreviewable. The Administrative Procedure Act deprives courts of jurisdiction where "agency action is committed to agency discretion by law." 5 U.S.C. § 701(a)(2). The Supreme Court of the United States has interpreted this withdrawal of jurisdiction as predicated on a showing that nonreviewability must "fairly be inferred," from the regulatory framework, *Barlow* v. *Collins*, 397 U.S. 159, 166, 90 S. Ct. 832, 837, 25 L. Ed. 2d 192 (1970), and that the statutes are drawn such that "there is no law to apply." *Citizens to Preserve Overton Park* v. *Volpe*, 401 U.S. 402, 410, 91 S. Ct. 814, 820, 28 L. Ed. 2d 136 (1971).

Whether a statute is drawn so broadly that there is no law to apply "turns on pragmatic considerations as to whether an agency determination is the proper subject of judicial review." *Natural Resources Defense Council* v. *Securities and Exchange Commission*, 606 F.2d 1031, 1043 (D.C. Cir. 1979). In that decision, the Court of Appeals set out the proper focus of the inquiry:

> . . . we first identify as precisely as possible the aspects of the agency's action against which the challenge is brought. We then evaluate the relevance of three particularly important factors: the need for judicial supervision to safeguard the interests of the plaintiffs; the impact of review on the effectiveness of the agency in carrying out its congressionally assigned role; and the appropriateness of the issues raised for judicial review. Finally, we inquire whether the considerations in favor of nonreviewability thus identified are sufficiently compelling to rebut the strong presumption of judicial review.

Id. at 1044 (citations omitted).

The exact agency action under attack in this case is the Board's ruling that the Glass-Steagall Act is not violated when a state member bank sells third party commercial paper. The Board attempts to characterize its decision as based on more

than a purely legal analysis, but this is just not the case. Although the Board solicited materials from Bankers Trust on its activities, it chose expressly not to rely on this factual material. In the Board's statement it concluded,

> Since, in the Board's opinion, the stronger argument is that commercial paper should not be treated as a security covered by the Glass-Steagall Act, the restrictions of the Act with regard to issuing, underwriting, selling, and dealing in securities do not apply. Thus, it is not necessary to reach the issue of whether the activities engaged in by Bankers Trust are prohibited by the Act.

R. At 688. Notwithstanding the Board's reliance on its special knowledge of the commercial paper market, once it decided not to address any factual matters underlying Bankers Trust's activity, it transformed the proceeding into a purely legal inquiry. Thus, the background of this dispute is materially different from that faced in *New York Stock Exchange* v. *Bloom*, 562 F.2d 736 (D.C.Cir. 1977), *cert. denied* 435 U.S. 942, 98 S.Ct. 1520, 55 L.Ed.2d 538 (1978), where the Court of Appeals decided to dismiss as unfit for review a petition seeking reversal of a decision of the Comptroller of the Currency that a specific automatic stock-investment plan did not violate the Glass-Steagall Act. In that case, the Court expressly noted that the Comptroller had assessed factual matters beyond a mere interpretation of the Act. But the Court was explicit as to how a pure legal question would be presented: "No doubt determining the general interest of Congress from the language and history of the Act is a matter of law. . . ." *Id.* at 741. A perusal of the Board's statements associated with its decision reveals that the Board resolved just a legal question in response to the Becker and SIA petitions. A weighing of the factors then set out in *Natural Resources Defense Council*, *supra*, leaves little doubt that the question presented is not only appropriate for review, but also demands judicial oversight in order to render a proper statutory interpretation.

Although the Board had discretion to make its legal decision, that discretion is neither absolute nor unreviewable. Rather, it represents the sort of administrative adjudication that has been held reviewable in the federal courts for "legal error, procedural defect or abuse." L. Jaffe, *Judicial Control of Administrative Action 362-63 (1965)*. *See Nader* v. *Saxbe*, 497 F.2d 676, 679-80 n. 19 (D.C.Cir. 1974). In *Natural Resources Defense Council*, it was noted that the Administrative Procedure Act itself "command[s] an exacting judicial scrutiny" of agency determinations of "pure questions of law." 606 F.2d at 1048. *See* 5 U.S.C. §§ 706(2)(B),(C),(D). It is difficult to imagine an issue more suited to judicial review than the Board's determination; indeed, the Board's contentions on the merits of this litigation are predicated almost wholly on canons of statutory interpretation and an analysis of legislative history, which belie its claim that there is no law to apply. Moreover, the Board made no showing that review in this case would hamper its effectiveness in the future. It merely maintained that courts should not direct that a specific enforcement tool be chosen, and that the statute's lack of guidance as to when a cease and desist order is appropriate should be respected. Although it is true that § 1818 offers scant direction governing when the Board should institute cease and desist proceedings, whether the Board's legal conclusion is proper rests on inquiries familiar to all courts.

Further, the Board's suggestion that nonreviewability can fairly be inferred from the statutory framework is flawed. Defendants contend that § 1818(b)(1) suggests that courts should not interfere in actions such as this. That section provides that "[i]f in the opinion of the appropriate . . . agency, any insured bank" has violated the law or engaged in an unsafe practice, "the agency may issue" a notice of charges to initiate enforcement proceedings." This section neither expressly nor impliedly affects the review of purely legal determinations. It merely leaves the Board with discretion to decide when to initiate enforcement proceedings. The Board's characterization of its discretion sweeps too broadly, because it attempts to apply this narrowly drawn enactment to insulate

from review any ruling on a wholly legal issue as long as the decision is somehow related to the institution of enforcement actions.[6]

The parties' positions as to the exact nature of the Board's action are not entirely illuminating because, in one sense, they are all only partially accurate. The plaintiffs assert (and it would be difficult to contravene), that the Board issued a ruling on a question of law, *i.e.*, that state member banks, under the Glass-Steagall Act, could permissibly sell third party commercial paper. The Board correctly notes, though, that this decision was pronounced in the context of deciding whether to initiate cease and desist proceedings against Bankers Trust. Neither the judicial nor the administative processes provide for decisions on legal questions in a vacuum; each dispute is occasioned by factual developments that give rise to a particular problem. The difficulty courts face is in effectuating the delicate balance between the smooth exercise of administrative discretion in areas where agencies have expertise and the right of a party aggrieved with an administrative agency's interpretation of a legal question to seek judicial review.

The statutory scheme created in § 1818 precludes judicial interference in the enforcement processes until the appropriate stage, but nothing in § 1818, nor even in traditional canons of administrative law, prevents this Court from reviewing the propriety and correctness of the Board's legal determination that state member banks may sell third party commercial paper.[7] To hold that jurisdiction is absent here would be to vest

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6 The parties briefed and argued the question whether the Board's decision was ripe for resolution in this Court because, at the time the motions were filed, the Board had not issued the promised guidelines to guard against what it thought to be potential unsafe practices resulting from a state member bank's sale of third party commercial paper. When these guidelines were issued, however, *see n.* 3, *supra* [197A], this issue evaporated from this controversy and hence will not be addressed.

7 This decision by the Board will undoubtedly have far reaching effect, much broader than merely permitting Bankers Trust to continue its commercial paper activity. The Board itself, as it issued guidelines

the Board with unreviewable discretion in any proceeding, limited only to facts presented, to resolve broad legal questions that are particularly within the competence of the courts to decide. Since the Court may not intrude into the congressionally sanctioned enforcement procedures set out in § 1818, and cannot therefore enjoin the Board to institute cease and desist proceedings, the Court's authority is restricted to resolution of the legal question presented and the grant of equitable relief consonant with that decision, within the bounds of appropriate judicial review.[8]

Before proceeding to consider the substance of the Board's conclusion, the parties vociferously dispute the degree of deference to be given the Board's expertise in the regulation of commercial banking in the United States. The Board suggests that its decision is immune from judicial alteration unless arbitrary, capricious, or wholly irrational. Plaintiffs contest this claim, pointing out that they challenge the Board's ruling on a legal question, reversal of which is mandated by the Administrative Procedure Act if not in accordance with the statute. 5 U.S.C. § 706.

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for all banks to follow, recognized that many banks were likely to adopt the route of Bankers Trust.

8 Although not raised by the parties, one final point on the jurisdictional issue warrants mention. In *Becker I*, the Court found that the Board's closure of its meetings on the petitions of *Becker* and *SIA* satisfied exemption 10 of the Sunshine Act, 5 U.S.C. § 552b(c)(10), which permits an agency to refuse to open a meeting concerning a decision to participate in adjudicatory proceedings, because the possibility of cease and desist proceedings was raised and discussed. That finding does not foreclose the determination that the matter on review at this time is the legal determination reached by the Board in conjunction with its decision not to initiate an action against Bankers Trust. The part of the Board's decision which rejected any enforcement proceeding against Bankers Trust is not subject to review, and to the extent that it was likely that proceedings against Bankers Trust might be discussed at the meetings, the Court remains convinced that the meetings were properly closed. That cease and desist proceedings may have been mentioned, however, does not assault the Court's authority to review the Board's resolution of the legal question at issue herein.

Amidst these opposing contentions the Court of Appeals has recently reaffirmed the Court's delicate role in deciding cases such as these:

> We are fully aware of the deference due the construction placed on a statute by an agency charged with the responsibility for administering it. . . . However, to accord deference is not to abdicate our duty to construe the statute, for the "courts are the final authorities and 'are not obliged to stand aside and rubber-stamp their affirmance of administrative decisions that they deem inconsistent with a statutory mandate or that frustrate the congressional policy underlying a statute.' "

National Association of Recycling Industries, Inc. v. *Interstate Commerce Commission*, 660 F.2d 795 at 798-99 (D.C.Cir., 1981). Specifically with regard to federal banking legislation, the Supreme Court has recognized the expertise of the Board in interpreting and administering that statute. *See Board of Governors* v. *Agnew*, 329 U.S. 441, 450, 67 S.Ct. 411, 415, 91 L.Ed. 408 (1947). Nonetheless, the duty to examine the Board's rule to ensure its accordance with the law cannot be shirked. In *National Distributing Co.* v. *United States Treasury Department*, 626 F.2d 997 (D.C.Cir. 1980), the Court noted,

> This Court is vested by statute with the authority and responsibility to "decide all relevant questions of law, interpret constitutional and statutory provisions, and determine the meaning or applicability of the terms of an agency action.". . . We are required to "hold unlawful and set aside agency action, findings, and conclusions found to be . . . not in accordance with the law[.]"

Id. at 1019, *quoting* the Administrative Procedure Act, 5 U.S.C. § 706.

Some illumination of the statutory framework surrounding this litigation is appropriate. The Glass-Steagall Act was part of a package of banking reforms passed during the early part of the Presidency of Franklin Delano Roosevelt. Two of its sections are pertinent to this dispute:

Section 16 (12 U.S.C. § 24) Corporate Powers of Associations

Seventh. . . . The Business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the *association shall not underwrite any issue of securities or stock: Provided,* That the association may purchase for its own account investment securities under such limitations and restrictions as the Comptroller of the Currency may by regulation prescribe. . . . As used in this section the term "investment securities" shall mean marketable obligations, evidencing indebtedness of any person, copartnership, association or corporation in the forms of bonds, notes and/or debentures commonly known as investment securities under such further definition of the term "investment securities" as may be prescribed by the Comptroller of the Currency.

* * * * * * * *

Section 21 (12 U.S.C. § 378) Dealers in securities engaging in banking business; individuals or associations engaging in banking business; examinations and reports; penalties.

(a) After the expiration of one year after June 16, 1933, it shall be unlawful—

(1) For any person, firm, corporation, association, business trust, or other similar organization, *engaged in the business of issuing, underwriting, selling or distributing*, at wholesale or retail, or through syndicate participation, *stocks, bonds, debentures, notes, or other securities, to engage at the same time to any extent whatever in the business of receiving deposits* subject to check or to repayment upon presentation of a passbook, certificate of deposit, or other evidence of debt. . . . (Emphasis added).

These provisions are made applicable to state member banks by 12 U.S.C. § 355.

The plaintiffs contend that the Board's decision contravenes the plain meaning of the Glass-Steagall Act because Bankers Trust, an institution in the business of receiving deposits, is, in their view, selling or underwriting commercial paper, which the plaintiffs argue is a security.

The first question to be addressed, then, is whether commercial paper is in fact a "note or other security" for purposes of the Glass-Steagall Act. In its statement asserting several legal bases for accepting the General Counsel's opinion, and in this litigation, the Board has attempted to justify its decision that commercial paper was not included in the Glass-Steagall Act. Section 21, the Board argues, was not intended to prohibit traditional banking functions, and the sale by Bankers Trust of third party commercial paper resembles other banking functions such as the sale of notes and bankers' acceptances to other lenders and the issuance of certificates of deposits. A decision that commercial paper is included within the Act's prohibition would, the Board suggests, jeopardize a host of traditional banking functions. Additionally, the Board analyzed the transaction involved in the sale of third party commercial paper and concluded that such activity resembled a loan, not a sale of securities. Although Congress did not, in 1933, specifically allude to commercial paper in the proceedings over Glass-Steagall, the Board points to indirect evidence that commercial paper was not intended to be included in the definition of "notes or other securities."

Plaintiffs maintain that the plain meaning of the Glass-Steagall Act prohibits exactly what Bankers Trust is doing, mixing the business of banking with the commerce of dealing in securities. The plaintiffs characterize the defendant's "parade of horribles" as irrelevant, because the traditional activities referred to by the Board are specifically permitted by other sections of the banking laws. In the plaintiffs' view what distinguishes Bankers Trust's conduct from other, more traditional banking functions, is the unique role of Bankers Trust, functioning between the issuer and the purchaser of commer-

cial paper. That role, the plaintiffs contend, is precisely what Congress intended to eliminate by its strict separation of investment banking from normal depository banking. Further, plaintiffs reject the Board's "functional anaylsis" that commercial paper is much like a loan, contending that the Board ignored the role of the bank in examining the transaction between the issuer of commercial paper and the purchaser. The plaintiffs also focus on the legislative history of the Glass-Steagall Act to support their position, citing, too, the Securities Act of 1933, which defines "securities" explicitly to include commercial paper. The Congress, plaintiffs proclaim, plainly sought to separate all dealing in speculative and other investments from the normal, more stable business of banking.

All statutory analysis begins with the recognition of an essential truth: "In any case concerning the interpretation of the statute, the 'starting point' must be the language of the statute itself, *Lewis* v. *United States*, 445 U.S. 55 [100 S.Ct. 915, 63 L.Ed.2d 198] (1980). . . ." *National Association of Recycling Industries, Inc.* v. *Interstate Commerce Commission*, 660 F.2d 795 at 799 (D.C.Cir. 1981). *See also Aaron* v. *Securities and Exchange Commission*, 446 U.S. 680, 100 S.Ct. 1945, 64 L.Ed.2d 611 (1980). Also entrenched in statutory interpretation is the principle that where a statute is not ambiguous, the party attempting to avoid its plain language must offer "persuasive reasons" for concluding that Congress did not mean what it said. *Higgins* v. *Marshall*, 584 F.2d 1035, 1037 (D.C.Cir. 1978), *cert. denied*, 441 U.S. 931, 99 S.Ct. 2051, 60 L.Ed.2d 659 (1979). *See Tennessee Valley Authority* v. *Hill*, 437 U.S. 153, 98 S.Ct. 2279, 57 L.Ed. 117 (1978). The plain meaning of a statute may be avoided where there has been a significant change of circumstances since enactment or when a literal reading leads to an unreasonable or absurd result. *Consumers Union of the United States, Inc.* v. *Heimann*, 589 F.2d 531, 534 (D.C.Cir. 1978).

What does a "plain" reading of the Glass-Steagall Act then reveal? Defendants cannot and do not seriously dispute that commercial paper is a "note or other security" as mentioned in Section 21. The parties agree that commercial paper consists of

short-term, negotiable, usually prime quality and unsecured notes. That under a strict reading of the Act, commercial paper would be covered by Section 21 is bolstered by the Court in *Investment Company Institute* v. *Camp*, 401 U.S. 617, 91 S.Ct. 1091, 28 L.Ed. 2d 367 (1971) (hereinafter *ICI I* or *Camp*) that "[t]here is nothing in the phrasing of either § 16 or § 21 that suggests the narrow reading of the word 'securities.' To the contrary, the breadth of the term is implicit in the fact that the antecedent statutory language encompasses not only equity securities but also securities representing debt." *Id.* at 635, 91 S.Ct. at 1101. Indeed, the statutes' unambiguous reference to "notes and *other* securities" surely indicates Congress's interpretation that the term "securities" encompassed "stocks, bonds, debentures and notes" in section 21. This meaning ascribed to section 21 applies with equal force to section 16, which does not mention "notes," but refers rather to "securities or stocks." *See Fortin* v. *Marshall*, 608 F.2d 525, 528 (1st Cir. 1979) (giving same words identical meanings in a single statute).

Does this strict interpretation of the Glass-Steagall Act lead to absurd and outrageous results? In the Board's view, many traditional commercial banking functions would simply grind to a halt were this Court to rule for plaintiffs, but their fears appear greatly exaggerated. Section 16 of the Glass-Steagall Act clearly recognizes that banks may discount and negotiate promissory notes as part of their traditional lending functions. Moreover, this Court is not presented with a broad-scale attempt by plaintiffs to reorganize the entire commercial banking industry. Rather, holding commercial paper to be included in the prohibition of the Glass-Steagall Act yields no great damage to the foundation of commercial banking. Whatever the Board decides to undertake as a result of the declaration herein is neither predicted nor directed, but when it recognizes that third-party commercial paper is a "note or other security," its mandate under the law will have been fulfilled.[9]

9 The Board decided that commercial paper was not an investment security and then swept to the conclusion that if the Court held that commercial paper was a note or security, banks would be completely

Reliance on the literal language of sections 16 and 21 is supported by the 1971 decision in *ICI I*. In *Board of Governors of the Federal Reserve System* v. *Investment Company Institute*, 450 U.S. 46, 101 S.Ct. 973, 67 L.Ed.2d 36 (1981) (hereinafter "*ICI II*") Mr. Justice Stevens described the *Camp* decision:

> In *Camp* the Court *relied squarely on the literal language of §§ 16 and 21 of the Glass-Steagall Act*. After noting that § 16 prohibited the underwriting by a national bank of any issue of securities and the purchase for its own account of shares of stock of any corporation, and that § 21 prohibited corporations from both receiving deposits and engaging in issuing, underwriting, selling, or distributing securities, *the Court recognized that the statutory language plainly applied* to a bank's sale of redeemable and transferable "units of participation" in a common investment fund operated by the bank.

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precluded from purchasing commercial paper. This, the Board contends, is an absurd result justifying rejection of the plain statutory language. The Board's contention that commercial paper is not an investment security, however, is not persuasive.

Section 16 grants to the Comptroller of the Currency the discretion to classify some securities as investment securities to permit banks to purchase them for their own account. The Comptroller's regulations specify that an investment security is "a marketable obligation in the form of a bond, note, or debenture which is commonly regarded as an investment security" that is not "predominately speculative in nature." 12 C.F.R. § 1.3(b). The Bank points to the legislative history of the McFadden Act of 1927 where Congressman McFadden clearly states that commercial paper was not considered an investment security. *See* 67 Cong. Rec. 3232 (1926). Plaintiffs indicate, however, that the McFadden Act was eviscerated by the Glass-Steagall Act in that Congress rejected the notion that commercial banks could be engaged in the investment banking business, a premise recognized by the McFadden Act. Additionally, plaintiffs submitted a letter from the Chief National Bank Examiner, dated March 10, 1981, in a matter unrelated to this dispute, where it is held that what is a loan for one purpose may be a security for another. Becker Reply Mem., Exh. 3. Banks could, even in light of the Court's holding, continue to purchase commercial paper as they traditionally have, and plaintiffs' arguments do not appear inconsistent with the scheme of the Glass-Steagall Act.

Id., 101 S.Ct. at 986 (emphasis added). See generally Clark and Saunders, *Judicial Interpretation of Glass Steagall: The Need for Legislative Action*, 97 Banking L.J. 721 (1980) (noting that courts traditionally invoke a literal interpretation of the Glass-Steagall Act).

The broad framework of the Glass-Steagall Act demonstrates that Congress intended to pass a flat prohibition against any single type of institution—commercial or investment banking—from engaging in any of the badges incident to the others' enterprise. The statute draws broad lines, leaving no room for administrative amendment. It reflects "the unalterable and emphatic intention of Congress to divorce commercial banks from the business of underwriting and dealing in securities." *Baker, Watts & Co.* v. *Saxon*, 261 F.Supp. 247, 252 (D.D.C. 1966), *aff'd sub nom. Port of New York Authority* v. *Baker, Watts & Co.*, 392 F.2d 497 (D.C. Cir. 1968). Deemed a "drastic step," the Glass-Steagall Act prohibits "commercial banks, banks that receive deposits subject to repayment, lend money, discount and negotiate promissory notes and the like, from going into the investment banking business." *ICI I*, 401 U.S. at 629, 91 S.Ct. at 1098. The Act "was a prophylactic measure directed against conditions that the experience of the 1920's showed to be great potentials for abuse." *Id.* at 639, 91 S.Ct. at 1103. The Court in *ICI I* further applied "as they were written" the Act's "literal terms" to overturn a decision of the Comptroller of the Currency to permit commercial banks to operate investment funds. *Id.*

This reading of the Glass-Steagall Act's framework is different from the Bank Holding Company Act of 1956, analyzed by the Supreme Court in *ICI II*. That statute authorizes the Board to determine whether a given activity is sufficiently related to banking to permit a nonbanking subsidiary of a bank holding company to engage therein. *See ICI II*, 450 U.S. at 73, 101 S.Ct. at 990. The Bank Holding Company Act clearly provides for the sort of discretionary decision made by the Board in this dispute, as it might be applied to a subsidiary of a bank holding company. But nowhere in the Glass-Steagall Act is the Board authorized, despite the plain language of the

statute, to permit a bank to engage in a particular activity because it does not pose risks to consumers or investors. Indeed, as the Court in *ICI I* recognized,

> From the perspective of competition, convenience, and expertise, there are arguments to be made in support of allowing commercial banks to enter the investment banking business. But Congress determined that the hazards [of that choice] made necessary to prohibit this activity to commercial banks.

ICI I, 401 U.S. at 636, 91 S.Ct. at 1101. Indeed, with the exception of the delegation in Comptroller of the Currency to determine what is an "investment security," there are no lines to be drawn.

The parties delve into the legislative history of the Glass-Steagall Act, neither producing convincing evidence of how Congress might have answered the question posed by this case were it presented in 1933. Nowhere in the record of the Act do the drafters define whether commercial paper is a note or other security. The defendants suggest that the Congress recognized that transactions in commercial paper were part of traditional banking practices at the time the Act was passed, and not part of the speculative business that gave rise to the prohibitions contained in the Act. Indeed, Senator Glass, whose name the Act bears, proposed during a debate on the Securities Act of 1933 that short term notes, including "nine months' commercial paper," be excluded from the definition of security contained in that legislation because such a definition would "radically interfere" with "ordinary commercial banking transactions." *Securities Act: Hearings on S. 875 before the Senate Committee on Banking and Currency*, 73d Cong., 1st Sess. 98 (1933). Plaintiffs counter that although banks were traditionally large purchasers of commercial paper, their role as seller was limited to occasional transactions; indeed, Congress's rejection of Senator Glass's proposal demonstrates a view that commercial paper was considered a security. It is unnecessary to trace the historical development of the commercial paper market; rather, based on the undisputed facts, the

role of Bankers Trust in its commercial paper transactions is an uncommon one for traditional banking institutions. Congress's silence as to commercial paper specifically, combined with the general scheme of the Act, indicates that it did not contemplate adjustments in the definition of "notes or other securities" by the Board or any other agency in an administrative proceeding.

The parties energetically dispute whether the definition of security in the Securities Act of 1933, which includes "any note," 15 U.S.C. § 77b(1), affects the interpretation of the Glass-Steagall Act. Although short term notes such as commercial paper are exempt from the registration provisions of the Securities Act of 1933, the antifraud proscriptions still apply. *See* 15 U.S.C. §§ 77c(a)(3), 77l(2). Defendants contend that the statutes have such different general purposes that it would be unreasonable to impute the definition of security offered in one statute to another act. *United Shoe Workers of America* v. *Bedell*, 506 F.2d 174, 188 (D.C.Cir.1974). Although the Securities Act of 1933 and the Glass-Steagall Act take regulatory aim at different financial institutions and markets, they were passed within three weeks of each other and designed to remedy the then existing catastrophe in the nation's financial markets. This is surely compelling evidence that the two statutes should be interpreted similarly. The district court, eventually affirmed in *ICI I* declared, "It would be inconsistent to conclude that Congress did not intend to obtain the equivalent meaning for the term 'securities' as used in the Securities Act of 1933 when it used the same term in the Glass-Steagall Act which was enacted by the same Congress." *Investment Company Institute* v. *Camp*, 274 F.Supp. 624, 642-43 (D.D.C.1967) (footnote omitted), *rev'd* 420 F.2d 83 (D.C.Cir. 1969), *rev'd* 401 U.S. 617, 91 S.Ct. 1091, 28 L.Ed.2d 367 (1971).

In an analogous decision, *United States* v. *American Building Maintenance Industries*, 422 U.S. 271, 95 S.Ct. 2150, 45 L.Ed.2d 177 (1975), the Supreme Court considered the phrase "in commerce" as it is used in the Federal Trade Commission Act and in the Clayton Act, and concluded that "since both sections were enacted by the 63d Congress, and both were

designed to deal with closely related aspects of the same problem—the protection of free and fair competition in the Nation's marketplaces," the statutes should be given similar interpretations. *Id.* at 277, 95 S.Ct. at 2155. Both the Glass-Steagall Act and the Securities Act were directed at curing the perceived rampant speculation by banks, securities dealers, and individuals prior to the Crash of 1929, such activity considered the chief cause of the Great Depression; their common goals suggest the relevance of the similar definitions.

The Board's final justification for its interpretation of the Glass-Steagall Act is its "functional analysis" of a commercial paper transaction which, in its view, compels the conclusion that commercial paper is more like a loan transaction than a security sale. The Board found that commercial paper, as short-term notes, functioned to provide corporations with cash and that banks, as traditional purchasers of commercial paper, effectively loaned such money to the issuers. *See* R. 682-84. The problem with the Board's analysis emerges instantaneously: it ignores the specific conduct of the bank, glossing over whether the bank purchases commercial paper for its own account, *e.g.*, its trust department, or purchases for future sale to an outside party or arranges a transaction between purchaser and seller. The Board's analysis would also sweep into its coverage almost all devices used by businesses to raise capital—including stocks and bonds—transforming transactions unquestionably at the heart of the securities industry into permissible activity for commercial depository banks. The dispute over the Board's determination that commercial paper represents a loan reveals the problematic query presented in this challenge: when is a device to raise funds for a business a loan and when is it a security? One factor present in this matter compels the conclusion that the commercial paper at issue here is not a loan, and that crucial aspect is the role of Bankers Trust in the transactions.[10]

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10 The Court, like the Board, does not reach the question whether Bankers Trust was actually underwriting securities in violation of the Glass-Steagall Act. The question presented herein is whether the Board

This dispute is only the proverbial tip of the iceberg as to debates currently raging in the houses of Congress concerning the proper functions of commercial banks, especially in light of a more active "banking" role taken by securities' dealers. In its *amicus* memoranda, the Securities and Exchange Commission argues forcefully and persuasively that any alteration of the lines drawn by current banking statutes is for the popularly-elected Congress to undertake. Especially in light of these current efforts to reallocate the roles of depository and non-depository institutions, both the Court and the Board should refrain from unique and heretofore unprecedented interpretations of the 1933 Glass-Steagall Act which cast such a long shadow as does the Board's ruling on the Becker and SIA petitions. The realignment of our nation's financial industries is for the elected representatives of our nation to bring to fruition by comprehensive legislation, and not for fiat by judicial decree or by administrative policymaking.[11]

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erred when it concluded that commercial paper was not a security under the Act. Although the Court has offered various characterizations to Bankers Trust's conduct, by no means does this opinion mean to convey that the bank was underwriting securities.

11 Becker contends that it was denied procedural due process by the Board in that the Board denied its request for a hearing or oral argument and refused to provide advance notice to Becker of the Board's meetings. The Court, in *Becker I* has already ruled on the open meeting aspect of the litigation, and Becker had no absolute right to present an oral argument. All of the written materials submitted were sufficient to permit the Board to deny oral argument without abusing its discretion. *Arthur Lipper Corp.* v. *Securities and Exchange Commission*, 547 F.2d 171, 182 n.8 (2d Cir. 1976), *cert denied*, 434 U.S. 1009, 98 S.Ct. 719, 54 L.Ed.2d 752 (1978). Becker also argues that the Board received *ex parte* communications from Bankers Trust while it was deliberating on the Becker and SIA petitions. The Board proffers an affidavit of Rose L. Arnold, in charge of the Freedom of Information Office for the Board, who indicates that the material received from Bankers Trust was available for inspection in the public reading room of the Board. Its availability to Becker and to the public negates Becker's contention that this material (now a part of the administrative record, *see* R. at 476-550) was concealed or that the Board's receipt of such documents prejudiced Becker's rights.

A word need be added about the exact nature of the relief to be awarded plaintiffs. As previously noted, the law prohibits any court from affecting the issuance of a cease and desist order under 12 U.S.C. § 1818. The plaintiffs have indicated that the principal relief sought is a declaratory judgment that the Board's September 26, 1980 ruling that commercial paper is not a note or security under the Glass-Steagall Act is contrary to law. Such a judgment is within the province of this Court to award, and is attached herein. The Court expresses no opinion as to what steps, if any, may be taken following the issuance of this declaratory judgment.

Opinion of the United States Court of Appeals for the District of Columbia Circuit

UNITED STATES COURT OF APPEALS
DISTRICT OF COLUMBIA CIRCUIT

Nos. 80-2258, 81-2070, 81-1493, 81-2058, 81-2096 and 80-2314

Argued 3 June 1982
Decided 2 Nov. 1982
As Amended Nov. 2, 1982

A.G. BECKER INCORPORATED,
Petitioner-Appellee,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,
Respondents-Appellants.

SECURITIES INDUSTRY ASSOCIATION,
Petitioner-Appellee,

—v.—

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, et al.,
Respondents-Appellants.

APPEARANCES:

Richard M. Ashton, Washington, D.C., with whom Michael Bradfield, Washington, D.C., was on the brief for Bd. of Governors of the Federal Reserve System, et al., appellants Nos. 81-2058 and 81-2070 and appellants/respondents in Nos. 80-2258, 80-2314, 81-1493 and 81-2096, James V. Mattingly, Jr., Washington, D.C., also entered an appearance for the Bd. of Governors of the Federal Reserve System, et al.

James B. Weidner, New York City, with whom John M. Liftin, Washington, D.C., was on the brief for Securities Industry Ass'n., petitioner in No. 80-2314 and appellee in No. 81-2058. Janet R. Zimmer, Washington, D.C., also entered an appearance for Securities Industry Ass'n.

Harvey L. Pitt, Washington, D.C., with whom Henry A. Hubschman and Andrea Newmark, Washington, D.C., were on the brief for A.G. Becker Inc., petitioner in No. 80-2258, appellants in Nos. 81-2096 and 81-1493 and appellee/respondent in No. 80-2070. James H. Schropp, Washington, D.C., also entered an appearance for A.G. Becker Incorporated.

Robert S. Rifkind, New York City, entered an appearance for New York Clearing House Ass'n, amicus curiae in Nos. 81-1493, 81-2258 and 81-2096.

Charles F.C. Ruff, U.S. Atty., Royce C. Lamberth, Kenneth M. Raisler, William H. Briggs, Jr., Asst. U.S. Attys., Washington, D.C., also entered an appearance for appellee/respondent in No. 81-1493.

John W. Barnum and W. Michael Tupman, Washington, D.C., entered appearances for Bankers Trust Co., amicus curiae in Nos. 80-2314, 81-2058, 80-2258, 81-1493, 81-2096 and 81-2070.

Leonard H. Becker, Steven A. Musher and Joseph McLaughlin, Washington, D.C., entered appearances for Goldman, Sachs and Co., amicus curiae in Nos. 80-2314, 81-2058, 80-2258, 81-1493, 81-2096 and 81-2070.

Paul Gorson and Russell Stevenson, Washington, D.C., entered appearances for Securities and Exchange Com'n, amicus curiae in Nos. 81-2096 and 81-2058.

Before TAMM and WILKEY, Circuit Judges and ROBB, Senior Circuit Judge.

Opinion for the Court filed by Circuit Judge WILKEY.

Dissenting opinion filed by Senior Circuit Judge ROBB.

WILKEY, *Circuit Judge*:

This case calls upon us to decide whether the Federal Reserve Board acted lawfully in permitting the Bankers Trust Company, a state member bank of the Federal Reserve System,[1] to act as agent in the sale of commercial paper. After Bankers Trust began marketing commercial paper, A.G. Becker, Inc., a broker-dealer in securities, and the Securities Industry Association ("SIA"), an organization representing over five hundred securities brokers and dealers, requested the Board to declare Bankers Trust's activities illegal and to bring appropriate enforcement action. Becker and the SIA contended that Bankers Trust was in violation of sections 16 and 21 of the Glass-Steagall Act ("the Act"), which prohibit commercial banks, with certain exceptions, from buying, selling, or underwriting "securities."[2] The Federal Reserve Board determined, however, that the commercial paper marketed by Bankers Trust

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1 *See* 12 U.S.C. §§ 321-339 (1976 & Supp. IV 1980).

2 Section 16 of the Act provides in pertinent part:

> The business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the association shall not underwrite any issue of securities or stock; *Provided*, That the association may purchase for its own account investment securities under such limitations and restrictions as the Comptroller of the Currency may by regulation prescribe.

12 U.S.C. § 24 Seventh (Supp. IV 1980).

Section 21 provides that:

> [I]t shall be unlawful . . . [f]or any person, firm, corporation, association, business trust, or other similar organization, engaged in the business of issuing, underwriting, selling, or distributing, at wholesale or retail, or through syndicate participation, stocks, bonds, debentures, notes, or other securities, to engage at the same time to any extent whatever in the business of receiving deposits subject to check or to repayment upon presentation of a passbook, certificate of deposit, or other evidence of debt, or upon request of the depositor. . . .

12 U.S.C. § 378(a)(1)(1976).

was not a "security" within the meaning of the Act.[3] Becker and the SIA then brought suit in the district court, which held the Board's determination to be invalid.[4] The Board appealed, and we reverse.

I. FACTS

"Commercial paper" refers to prime quality, negotiable promissory notes bearing very short maturities—generally 30 to 90 days.[5] Large, financially strong corporations use commercial paper to obtain funds for current needs. Commercial paper is sold, in denominations averaging one million dollars or more, to large, sophisticated purchasers—money market mutual funds, bank trust departments, insurance companies and pension funds.[6]

Bankers Trust began placing third party commercial paper in 1978.[7] Its issuers had the highest rating from at least one of the rating services for commercial paper issuers; its customers were part of the bank's established base of institutional investors, who regularly purchase short term instruments from the bank. The bank offered to act as financial adviser to issuers of paper sold by the bank, and to extend credit to them, though for only

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3 Federal Reserve System, Statement Regarding Petitions to Initiate Enforcement Action (26 Sept. 1980), Joint Appendix (J.A.) at 220 [hereinafter cited as Federal Reserve Statement].

4 *A.G. Becker, Inc.* v. *Board of Governors*, 519 F. Supp. 602 (D.D.C. 1981).

5 *See generally* Hurley, *The Commercial Paper Market*, 63 Fed. Res. Bull. 525 (1977); Comment, *The Commercial Paper Market and the Securities Acts*, 39 U. Chi. L. Rev. 362 (1972).

6 *See* sources cited at *supra* note 5. *See also infra* p. 149 [245A].

7 This description of Bankers Trust's activities relies upon Federal Reserve Statement, *supra* note 3, at 2-3, J.A. at 221-22. Appellees do not challenge the Board's factual findings as to Bankers Trust's participation in the commercial paper market.

a small portion of the unsold amount of the issue. It did not commit itself to purchase unsold paper, but it did purchase in the secondary market commercial paper of issuers for which it had acted. Bankers Trust was the first commercial bank to enter the commercial paper market in competition with the investment banks; other commercial banks awaited the outcome of subsequent legal proceedings.

Becker and the SIA requested the staff of the Federal Reserve Board to review the legality of Bankers Trust's activities. The Board's general counsel, after extensive discussion with Becker, SIA, Bankers Trust and the SEC, issued an opinion declaring that commercial banks may lawfully act as agent for the issuer in the sale of commercial paper, "provided that the sales . . . are limited to purchasers to whom commercial banks normally sell participations in loans."[8] Becker and the SIA then requested the Federal Reserve Board to review the decision of its general counsel and to proscribe the commercial paper activities of member banks. After considering submissions by interested parties and conducting an on-site investigation of Bankers Trust's activities, the Board ruled that Bankers Trust's participation in the commercial paper market did not violate the Glass-Steagall Act or contravene public policy.[9]

In a carefully reasoned opinion the Board first concluded that there was no indication in the language or legislative history of the Glass-Steagall Act that Congress considered commercial paper to be a "security," in which banks were forbidden to deal.[10] The Board noted that banks had traditionally traded in commercial paper, and that the Act had been intended to strengthen banks in the exercise of traditional banking functions. The Board then turned to a "functional" analysis of the statutory terms, and concluded that, because

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8 Legal Division, Board of Governors of the Federal Reserve System, Commercial Paper Activities of Commercial Banks: A Legal Analysis 21 (28 June 1979), J.A. at 168.

9 Federal Reserve Statement, *supra* note 3.

10 *Id.* at 6-17, J.A. at 225-36.

commercial paper embodies short-term loans from a few sophisticated lenders to financially strong borrowers, it resembled a loan rather than a security for the purpose of the Glass-Steagall Act.[11] Because the Board ruled that commercial paper was not a "security," it did not reach the issue whether Bankers Trust was "issuing, underwriting, selling, or distributing" securities within the meaning of the Glass-Steagall Act.[12]

Subsequently, the Board issued guidelines to ensure that sale of third party commercial paper did not give rise to "unsafe or unsound practices."[13] These guidelines permitted banks to sell only prime quality third party commercial paper with maturity of nine months or less and in denominations of over $100,000. Banks could sell only to "financially sophisticated customers," and were forbidden to advertise to the general public. Sales to the bank's fiduciary accounts, parent holding companies and nonbank affiliates were also forbidden. Moreover, banks were required to maintain credit analyses of issuers, to limit the amount of paper sold for any issuer, and to maintain detailed records of sales, purchases and lines of credit extended. Finally, various disclosure requirements were imposed.

SIA and Becker sought review in the district court of the Board's ruling that commercial paper was not a "security." That court concluded that the Act's "plain language" barred commercial banks from trading in commercial paper.[14] It also found that the "broad framework" of the Act evinced Con-

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11 *Id.* at 17-20, J.A. at 236-39. The Board also rejected the arguments that the definition of "security" in the Securities Act of 1933, or considerations of public policy, militated against permitting Bankers Trust's sale of third party commercial paper. *Id.* at 20-27, J.A. at 239-46.

12 *Id.* at 24, J.A. at 243.

13 Policy Statement Concerning the Sale of Third Party Commercial Paper by State Member Banks, 46 Fed. Reg. 29333, 29334-35 (26 May 1981) [hereinafter cited as Guidelines].

14 *Becker*, 519 F. Supp. at 612-13.

gress' intent to institute a sweeping prohibition of commercial banks' engaging in investment banking activities.[15] Finally, in response to the Board's "functional" analysis of commercial paper, the court averred that "[o]ne factor . . . compels the conclusion that the commercial paper at issue here is [a security], and that crucial aspect is the role of Bankers Trust in the transaction."[16] For these reasons, the district court issued a declaratory judgment that the Board's ruling was contrary to law.[17]

We reverse. The district court gave insufficient weight to the expertise of the Federal Reserve Board—as the agency responsible for administering the nation's banking system—in interpreting the provisions of the Glass-Steagall Act. Moreover, the language of the Act, its legislative history and the policies underlying it all support the Board's conclusions that commercial paper is not a "security" under the Act. We discuss each of these findings in turn.

II. STANDARD OF REVIEW

The Supreme Court recently had occasion again to delineate the standard to be applied in the review of an agency's interpretation of a statute which it is charged to implement.

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15 *Id.* at 614-15.

16 *Id.* at 615-16.

17 *Id.* at 616. The district court confined its holding to the question of whether the commercial paper at issue was a "security." Like the Board, it did not reach the question whether Bankers Trust was "underwriting" securities in violation of the Glass-Steagall Act. *See id.* at 616 n. 10.

Moreover, the district court did not explicitly rule on the validity of the Board's guidelines. However, because the guidelines in essence describe Bankers Trust's activities, it would be difficult to reconcile those guidelines with the district court's holdings. Conversely, if we find that Bankers Trust has acted lawfully, the activities of other commercial banks in compliance with the guidelines would be lawful as well. *See* Part IV (Conclusion) *infra*.

The task of the reviewing court is "not to interpret the statute as it [thinks] best but rather the narrower inquiry into whether the [agency's] construction was '*sufficiently reasonable*' to be accepted by a reviewing court. . . . To satisfy this standard it is not necessary for a court to find that the agency's construction was the only reasonable one or even the reading the court would have reached if the question initially had arisen in a judicial proceeding."[18]

In particular, the Board's ruling in the present case warrants deference for a number of reasons. First, the Board is "the type of agency to which deference should presumptively be afforded" because of *the scope of its authority*. Congress has vested the Board with "primary and substantial responsibility for administering" federal regulation of the national banking system.[19] The Board exercises "general supervisory" powers over member banks,[20] and is responsible to bring enforcement actions to prevent member banks from engaging in "unsafe or unsound" banking practices.[21] The Board thus formulates national banking policy, and, in implementing this policy, exercises broad rulemaking and adjudicative powers.

Second, deference to the Board's conclusions is warranted by its *expert knowledge of commercial banking*. "Not only because Congress has committed the [Federal Reserve] [S]ystem's operation to [the Board's] hands, but also because the system itself is a highly specialized and technical one, requiring expert and coordinated management in all of its phases, . . . their judgment should be conclusive upon any

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18 *Fed. Election Comm'n* v. *Democratic Senatorial Campaign Comm.*, 454 U.S. 27, 39, 102 S.Ct. 38, 46, 70 L.Ed.2d 23 (1981) (emphasis added) (citations omitted).

19 *Compare Democratic Senatorial Campaign Comm.*, 454 U.S. at 39, 102 S.Ct. at 46.

20 *See* 12 U.S.C. § 248 (1976).

21 *See* 12 U.S.C. § 1818(b) (Supp. IV 1980). *See also* 12 U.S.C. § 501a (1976) (enforcement actions for violation of banking laws and regulations).

matter which . . . is open to reasonable difference of opinion. Their specialized experience gives them an advantage judges cannot possibly have . . . in ascertaining the meaning Congress had in mind in prescribing the standards by which they should administer [the system]."[22]

Third, deference to an agency's construction of the statute is called for because *the agency's decision applies general, undefined statutory terms*—"notes and securities"—to particular facts. While the Glass-Steagall Act contains a sweeping prohibition of commercial banks' trading in "securities," that term is, of course, not self-defining.[23] Moreover, we cannot assume that Congress intended the term to comprise a set of rigid and unchanging categories. Rather, such statutory drafting "leave[s] the agency with the task of evolving definitions on a case-by-case basis."[24] The regulatory structure of the banking laws must be permitted to adapt to the changing financial needs of our economy.[25] Congress has delegated to the Federal Reserve Board, rather than to this court, the complex task of applying the Act's general proscriptions to current business reality. We must therefore defer to the Board's interpretation of the statute if that interpretation is reasonable.

22 *Board of Governors of the Federal Reserve System* v. *Agnew*, 329 U.S. 441, 450, 67 S.Ct. 411, 415, 91 L.Ed. 408 (1947) (Rutledge, J. concurring). *See Board of Governors of Federal Reserve System* v. *Investment Co. Inst.*, 450 U.S. 46, 56 n.21, 101 S.Ct. 973, 981 n.21, 67 L.Ed.2d 36 (1981) (citing *Agnew*) [hereinafter cited as *ICI II*].

23 *See infra* p. 143 [232A-235A].

24 *Puerto Rico* v. *Blumenthal*, 642 F.2d 622, 635 (D.C. Cir. 1980), *cert. denied*, 451 U.S. 983, 101 S.Ct. 2315, 68 L.Ed.2d 840 (1981); *Chisholm* v. *FCC*, 538 F.2d 349, 358 (D.C. Cir.), *cert. denied*, 429 U.S. 890, 97 S.Ct. 247, 50 L.Ed.2d 173 (1976).

25 *Cf. M & M Leasing Corp.* v. *Seattle First Nat'l Bank*, 563 F.2d 1377, 1382 (9th Cir. 1977), *cert. denied*, 436 U.S. 956, 98 S.Ct. 3069, 57 L.Ed.2d 1121 (1978) (bank laws construed to permit "use of new ways of conducting the very old business of banking"). The current situation of the commercial paper market could not have been foreseen by Congress at the time the Glass-Steagall Act was passed: that market has changed drastically since the Depression. *See infra* note 85.

Finally, "*the thoroughness evident in the consideration* [of an agency's interpretation of a statute], *the validity of its reasoning*, [and] *its consistency with earlier and later pronouncements*" are factors that bear upon the amount of deference to be given to an agency's ruling.[26] In this instance, the agency's interpretation of the statute is based on a thorough and expert review of the relevant legal and policy considerations as well as of the facts of this case. The Board conducted an extensive inquiry into the operation of Bankers Trust commercial paper operations and the function of the commercial paper market; it clearly set forth its findings, conclusions, and bases for its reasoning.[27] And the Board's conclusion is consistent with prior decisions, including some roughly contemporaneous with the passage of the Glass-Steagall Act.[28]

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26 *Skidmore* v. *Swift & Co.*, 323 U.S. 134, 140, 65 S.Ct. 161, 164, 89 L.Ed. 124 (1944) (emphasis added). *See Democratic Senatorial Campaign Comm.*, 454 U.S. at 39, 102 S.Ct. at 46 (citing *Swift*); *Adamo Wrecking Co.* v. *United States*, 434 U.S. 275, 287 n.5, 98 S.Ct. 566, 574 n.5, 54 L.Ed.2d 538 (1978) (same).

27 Federal Reserve Statement, *supra* note 3.

28 For example, in 1933 the Board stated that commercial paper, defined as short-term paper issued for obtaining funds for current transactions and purchased by banks and corporations with temporarily idle funds, should not be considered an investment security. *See Federal Securities Act: Hearing on H.R. 4314 before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 1st Sess. 180-81 (1933); *Securities Act: Hearings on S. 875 Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. 120 (1933); Federal Reserve Statement, *supra* note 3, at 11, J.A. at 230.

The assumption that commercial paper is a loan rather than a security pervades current banking regulation. The Board has ruled that issuance of commercial paper by a bank holding company does not fall within section 20 of the Glass-Steagall Act, the analogous provision for those companies. *See* 12 C.F.R. § 250.221(e)(1982). Under the rules of the Comptroller General's office, commercial paper holdings by banks are subject to the statutory limits on loans rather than investment securities. *See* 12 C.F.R. § 7.1180 (1982) (interpreting 12 U.S.C. § 84 (1976)); Federal Reserve Statement, *supra* note 3, at 11-12, J.A. at

For these reasons, which we have considered in prior opinions and which may frequently be found of use in evaluating administrative agency decisions, we should hesitate to overturn the Board's decision as long as that decision is a reasonable interpretation of the Glass-Steagall Act. And, as will appear below, the decision was reasonable. We do not, however, rest merely on the deference to the conclusions of the Federal Reserve Board. "[T]o accord deference is not to abdicate our duty to construe the statute, for 'the courts are the final authorities and are not obliged to stand aside and rubber-stamp their affirmance of administrative decisions that they deem inconsistent with a statutory mandate or that frustrate the congressional policy underlying a statute.' "[29] We therefore turn to an analysis of the application of the Glass-Steagall Act to the present case.

III. APPLICATION OF THE GLASS-STEAGALL ACT

Taking account of appropriate deference to the Board's expertise and administrative responsibility, we find that its ruling and the reasoning which supports it are essentially correct. An inquiry into the language and legislative history of the statute, and the policies underlying it, supports the Board's conclusion that the commercial paper marketed by Bankers Trust is not a "security" within the Glass-Steagall Act.

A. *Background*

Congress passed the Glass-Steagall Act in 1933, in response to what it perceived to be the abuses which resulted from the involvement of commercial banks in securities underwriting. Congress considered that commercial banks, by underwriting

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230-31. And commercial paper is treated as a loan for bank call reports and bank examination by the Federal Reserve Board. *Id.*

29 *Nat'l Ass'n of Recycling Inds., Inc.* v. *ICC*, 660 F.2d 795, 799 (D.C.Cir. 1981) (citations omitted).

stocks, had fueled the rampant speculation that preceded the Great Depression. Congress' principal concern in amending the banking laws, however, was to protect the solvency and integrity of the banks themselves.[30]

Stock underwriting by commercial banks undermined bank solvency in a number of ways. Most directly, commercial banks that engaged in underwriting tied up depositors' funds in the purchase of unsound or speculative securities. These investments placed commercial deposits at risk.[31] The promotional pressures exerted by underwriting activities also threatened bank solvency. To augment their commissions from securities sales, commercial banks used their credit facilities to lend to purchasers of securities.[32] Banks were also tempted to make unsound loans to client-issuers, because these loans might improve the balance sheet of these enterprises and thereby make their securities more marketable. When speculative ventures failed, these loans to purchasers and issuers were often not repaid, undermining bank solvency and depositor confidence in the banks.[33]

In addition to inducing commercial banks to purchase unsound securities and to make unsound loans, banks' participation in the securities market had more indirect effects on bank solvency. Banks' association with speculative securities ventures undermine the confidence of bank depositors in the stability of the banks.[34] Moreover, banks which underwrote

30 *Senate Comm. on Banking and Currency, Operation of the National and Federal Reserve Banking Systems*, S. Rep. No. 77, 73d Cong., 1st Sess. 2-4, 6-13 (1933).

31 *Id.* at 9-10.

32 *See* 75 Cong. Rec. 9912 (1932) (remarks of Sen. Bulkley); *Operation of the National and Federal Reserve Banking Systems: Hearings Pursuant to S.Res. 71 before a Subcomm. of the Senate Comm. on Banking and Currency*, 71st Cong., 3d Sess. 87 (1931) (remarks of Chairman Glass) [hereinafter cited as *Hearings*].

33 75 Cong. Rec. 9912 (1932) (remarks of Sen. Bulkley).

34 *Id.*

stock issues could not be relied upon to give prudent and disinterested investment advice to their depositors, for they naturally had an incentive to urge depositors to purchase shares of the issues the bank was underwriting.[35] Finally, these banks would also "dump" excess issues of unmarketable securities on their own trust departments.[36]

Congress passed the Glass-Steagall Act to correct these abuses. The Act is a prophylactic measure designed to prevent commercial banks from being exposed to the dangers which inevitably followed upon their participation in investment banking. "Congress acted to keep commercial banks out of the investment banking business largely because it believed that the promotional incentives of investment banking and the investment banker's pecuniary stake in the success of particular investment opportunities was destructive of prudent and disinterested commercial banking and of public confidence in the commercial banking system."[37]

B. *Statutory language*

Congress accomplished the separation of commercial and investment banking in sections 16 and 21 of the Glass-Steagall Act. We first ask whether the language of these sections clearly evinces a congressional determination to prohibit the activities in which Bankers Trust has engaged; if so, our inquiry necessarily comes to an end.[38]

Section 16 provides that a bank "shall not underwrite any issue of *securities or stock*" and shall not "purchase . . . for its own account . . . any *shares of stock* of any corpora-

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35 *Hearings*, *supra* note 32, at 237.

36 *Id.*

37 *Investment Co. Inst.* v. *Camp*, 401 U.S. 617, 634, 91 S.Ct. 1091, 1100, 28 L.Ed.2d 367 (1971) [hereinafter cited as *ICI I*].

38 *E.g.*, *Transamerica Mortgage Advisers, Inc.* v. *Lewis*, 444 U.S. 11, 16, 100 S.Ct. 242, 245, 62 L.Ed.2d 146 (1979).

tion."[39] We can find nothing in the language of this section that explicitly articulates a congressional intent to bar commercial banks from trading in commercial paper. The terms "securities" and "stock" are not defined by the Act; section 16 in no way refers explicitly to notes, the generic financial term which Congress might have used to encompass commercial paper.[40] Indeed, banks are authorized to "discount and negotiate promissory notes, drafts, bills of exchange, and other evidences of debt. . . ."[41] It is clear, then, that section 16 does not prohibit banks from selling or underwriting *all* notes, but *only* "securities or stock"; and the section does not indicate whether the commercial paper at issue in this case is included within that statutory prohibition.

We turn then to section 21 of the Act, which forbids banks from underwriting "stocks, bonds, debentures, notes, or other securities. . . ."[42] Although this statutory provision explicitly refers to "notes," that term is susceptible of at least two interpretations. First, it may refer to a specific type of long-term debt security, one that closely resembles a bond or debenture but is of shorter maturity.[43] A note in this sense, like a bond or a debenture, is issued under an indenture agreement to raise money available for an extended period of time as part of the corporation's capital structure. An investment note

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39 12 U.S.C. § 24 Seventh (Supp. IV 1980) (emphasis added). The Act allows for several exceptions; the one pertinent here is that for "investment securities." *See infra* pp. 145-146 [19a].

40 *See infra* p. 143 [234A] & note 44.

41 12 U.S.C. § 24 Seventh (Supp. IV 1980).

42 12 U.S.C. § 378(a)(1) (1976). If the language of *either* section 16 *or* section 21 must be interpreted to prohibit Bankers Trust's marketing of commercial paper, that interpretation of course governs. *See generally ICI II*, *supra*, note 22, 450 U.S. at 62-65, 101 S.Ct. at 984-86.

43 *See, e.g.*, 1 A. Dewing, The Financial Policy of Corporations 180 (4th ed. 1941); G. Munn, Encyclopedia of Banking and Finance 132 (7th ed. 1973).

differs from these other instruments in that it matures more quickly—in a few, rather than twenty or more, years.

Second, the term "notes" is sometimes used generically to refer to *any* promissory instrument regardless of maturity or negotiability.[44] In this sense, commercial paper may also be referred to as a promissory "note." Such a note differs sharply from an investment "note": commercial paper is used to obtain short-term credit for current transactions, rather than capital funds for long-term projects. Its maturity generally ranges from one to two months, and rarely exceeds nine months.[45]

The language of section 21 suggests that Congress intended only to prohibit the marketing of investment notes—*i.e.*, that it intended to use "notes" in its more specific meaning. Each of the terms listed by Congress—"stocks," "bonds," "debentures" and "notes"—refers to a specific type of long-term investment security.[46] In contrast, "notes" in the more general sense would also include financial instruments, such as commercial paper, which have little in common with these long-term investment securities.[47] Moreover, "notes" used in its

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44 *See, e.g.*, G. Munn, *supra*, note 37, at 698 (defining "note" as a "written promise . . . to pay a certain sum of money to the . . . payee").

45 *See also infra* p. 149 [245A] & note 80.

46 "Stocks," of course, represent ownership interests in a corporation. "Bonds" are secured debt instruments, issued under a trust indenture agreement, that bear long-term maturities and are offered to the public in small denominations. "Debentures" differ from bonds only in that they are unsecured.

47 *See Third Nat'l Bank in Nashville* v. *IMPAC, Ltd.*, 432 U.S. 312, 322 & n. 16, 97 S.Ct. 2307, 2313 & n. 16, 53 L.Ed.2d 368 (1977) ("words grouped in a list should be given related meanings"); *Am. Maritime Ass'n* v. *Stans*, 485 F.2d 765, 768 (D.C.Cir. 1973) (same). *Cf. Jarecki* v. *G.D. Searle & Co.*, 367 U.S. 303, 307, 81 S.Ct. 1579, 1582, 6 L.Ed.2d 859 (1961) (statutory term "gathers meaning from the words around it").

Similarly, under the familiar principle that where general words follow specific words in an enumeration, the general words are

more general sense would include debt instruments such as bonds and debentures; the explicit statutory reference to the latter would then be redundant.[48] For these reasons, specific inclusion of the terms "stocks," "bonds," and "debentures" suggests that the narrower meaning of the term "notes" was intended. We conclude that the context in which the term "notes" is used strongly implies Congress' intent not to include commercial paper within the sweep of the Act's prohibition.

Both section 16 and section 21 thus demarcate a fundamental division between notes which represent commercial banking

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construed to embrace only items similar to those specifically enumerated, *see, e.g., Harrison* v. *PPG Inds., Inc.*, 446 U.S. 578, 588, 100 S.Ct. 1889, 1895, 64 L.Ed.2d 525 (1980), the phrase "or other securities would include *only* financial instruments with the economic characteristics of those listed, *see supra* note 46, *not* commercial paper.

The conclusion that commercial paper differs markedly from those instruments which Congress intended to prohibit commercial banks from underwriting depends ultimately upon an analysis of the relevant economic characteristics of these instruments, such as the characteristics noted in text. It is clear that commercial paper differs from the family of specific instruments listed in section 21 of the Act; we explain below the relevance of these differences to the policies wich Congress intended the Act to advance. *See infra* parts IIIC (legislative history) and IIIE (functional analysis of the commercial paper market).

48 *See Ass'n of Am. R.Rs.* v. *United States*, 603 F.2d 953, 964 (D.C. Cir. 1979) (presumption that "Congress [does] not employ superfluous language").

A third reason to reject a broad definition of the term "note" is that this definition would include a number of instruments in which banks have traditionally traded—for example, certificates of deposit, notes evidencing a mortgage and notes representing commercial loans in connection with a loan syndication. All of these clearly involve a "written promise to pay a certain sum to the payee," *see supra* note 44; their sale by banks would therefore be prohibited by appellees' reading of the statute. Moreover, it makes little sense to argue, as do appellees, that we may escape this quandary by interpreting the Glass-Steagall Act to prohibit only banking practices not otherwise authorized by the banking laws: The banks may only exercise expressly granted powers in any event. *See, e.g., Arnold Tours, Inc.* v. *Camp*, 472 F.2d 427 (1st Cir. 1972); *Saxon* v. *Georgia Ass'n of Indep. Ins. Agents, Inc.*, 399 F.2d 1010 (5th Cir. 1968).

transactions—transactions which are, of course, permitted under the Act—and securities, such as investment notes, which commercial banks are prohibited from underwriting. Section 16 indicates this distinction by authorizing commercial banks to negotiate "promissory notes," while forbidding banks to negotiate "securities or stocks." Section 21 makes the distinction by barring banks from trading in specified instruments for raising capital as part of the permanent financial structure of a corporation—stocks, bonds, debentures and notes—while implicitly permitting transactions in other types of debt instruments. And the language of these sections, while not conclusive, strongly suggests that sale of commercial paper should be treated as a "loan" rather than a sale of securities for the purposes of the Act.

C. Legislative history

The distinction between commercial loans and securities emerges as well from an analysis of the legislative history. Throughout its debates on the causes of the imperiled state of the banking industry, Congress nowhere considered the banks' activity in the commercial paper market as contributing to their difficulties.[49] The commercial paper market was simply not part of the problem to which the Glass-Steagall Act was addressed.[50] Rather, Congress focused its attention on the commercial banks' participation in "speculative" securities markets: their extensive underwriting of long-term holdings of high risk stocks and bonds.

For example, the Senate Report on the Act notes that "[t]he outstanding development in the commercial banking system during the prepanic period was the appearance of excessive

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49 *See* Federal Reserve Statement, *supra* note 3, at 14-15, J.A. at 233-34.

50 This is particularly remarkable because, at the time the Glass-Steagall Act was passed, almost all commercial paper issued was purchased by commercial banks for their own account. *See* Hurley, *supra* note 5.

security loans, and of over-investment in securities. . . . [A] very fruitful cause of bank failures . . . has been the fact that the funds of various institutions have been so extensively '*tied up' in long-term investments.*"[51] Congress condemned "the excessive use of bank credit in making loans for the purpose of *stock speculation*. . . ."[52] In short, the purpose of the Act was to reverse "a loose banking policy which had turned from the making of loans on *commercial paper* to the making of loans on *security.*"[53]

The distinction between bank participation in the securities and in the commercial paper markets is also illustrated in Congress' treatment of section 2(b) of the McFadden Act.[54] Section 2(b) limited the amounts of "investment securities" national banks could hold.[55] It is clear, however, that *commercial paper was not considered an "investment security"* under the McFadden Act: banks were left free to trade in commercial

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51 S. Rep. No. 77, *supra* note 30, at 8 (emphasis added).

52 *Id.* at 9 (emphasis added).

53 *Id.* at 4 (emphasis added). The hearings and floor debates of the Act are also replete with evidence that Congress was concerned with banks' speculation in long-term equity and debt securities rather than with their participation in the commercial paper market. *See, e.g.*, 77 Cong. Rec. 3725, 3837 (1933) (remarks of Sen. Glass); *Hearings, supra* note 32, at 1006-19; *Operation of the National and Federal Reserve Banking Systems; Hearings on S. 4115 Before the Senate Comm. on Banking and Currency*; 72d Cong., 1st Sess. 146 (1932) (remarks of Sen. Glass); *id.* at 66-67 (remarks of president of American Bankers Association); 75 Cong. Rec. 9904 (1932) (remarks of Sen. Walcott); *id.* at 9911-12 (remarks of Sen. Bulkley) (promotional pressures encouraging over-development of collateral-security loans and over-production of capital securities).

54 Ch. 191, 44 Stat. 1224 (1927).

55 44 Stat. at 1226 (codified at 12 U.S.C. § 24 Seventh (Supp. IV 1980)). The Act restricted bank holdings of the securities of any one obligor to twenty-five percent of the bank's holdings. *Id.* The Glass-Steagall Act further restricted the permissible amounts of these holdings. Ch. 89, sec. 16, 53 Stat. 162, 185 (1933) (later modified).

paper without restriction.[56] It is significant, therefore, that Congress preserved the provisions of the McFadden Act when it passed the Glass-Steagall Act six years later.[57] The legislative history of the Glass-Steagall Act provides no indication that Congress intended to change the McFadden Act's definition of "investment security."[58] Moreover, it is unlikely that Congress would consider commercial paper to be a "security" but *not* an "investment security."[59] Thus, Congress' incorporation of the McFadden Act into the revised banking laws, like other aspects of the legislative history, indicates an intent to continue to leave banks free to deal in commercial paper.

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56 Federal Reserve Statement, *supra* note 3, at 9, J.A. at 228; 67 Cong. Rec. 3232 (1926); H.R. Rep. No. 83, 69th Cong., 1st Sess. 3-4 (1926). Congress was legislating to control national banks' underwriting activities, which had sprung up in the early 1900s. In contrast, these banks had dominated the commercial paper market since the middle 19th century. *See* Federal Reserve Statement, *supra* note 3, at 10, J.A. at 229; A. Greef, The Commercial Paper House in the United States at 6-7, 15-18, 403-05 (1938).

57 Ch. 89, sec. 16, 53 Stat. 162, 185 (1933).

58 *See* S. Rep. No. 77, *supra* note 30, at 16 (banks permitted to purchase and sell investment securities "to the same extent as heretofore").

59 The conclusion that commercial paper is not a "security" or "stock" would follow *a fortiori* from the conclusion that commercial paper is not an "investment security." If commercial paper is a security but not an investment security, banks would be entirely forbidden from purchasing, selling, or underwriting commercial paper, while permitted, subject to the regulation of the Comptroller of the Currency, to purchase or sell corporate debt instruments. This would be quite anomalous, for corporate debt instruments threaten to a far greater degree to cause the evils at which the Glass-Steagall Act is aimed. Moreover, if commercial paper were deemed to be a "note" within section 21 of the Glass-Steagall Act, it ought also to be a "marketable obligation[ ] evidencing indebtedness . . . in the form of [a] note[ ]"—*i.e.*, an "investment security"—under section 16. That the legislative history and administrative implementation of the McFadden Act indicate clearly that commercial paper is not an "investment security" implies therefore that it should not be considered a "note" for the purposes of the Glass-Steagall Act.

D. *The Analogy to the Securities Laws*

Plaintiffs suggest that we may infer Congress' intent from its use of the term "security" in two contemporaneous statutes—the Securities Act of 1933 and the Securities Exchange Act of 1934. Both acts define "security" to include "any note."[60] There is no reason, however, to assume that Congress intended that term to bear the same meaning in these different statutory contexts. Congress enacted the Glass-Steagall Act primarily to protect *bank depositors*.[61] By contrast, "[t]he primary purpose of the [Securities Acts] of 1933 and 1934 was to eliminate serious abuses in a largely unregulated securities market. The focus of the Acts is on the capital market of the enterprise system: the sale of securities to raise capital for profit-making purposes, the exchanges on which securities are traded, and *the need for regulation to prevent fraud and to protect the interest of investors*."[62]

Therefore, although Congress used the term "securities" in both the Glass-Steagall and the Securities Acts, different interpretations of "securities" may follow upon the differing regulatory purposes behind the Acts.[63] "Because securities transactions are economic in character Congress intended the application of [the Securities Acts] to turn on the *economic realities underlying a transaction*. . . ."[64] Similarly, the Court has defined the term "securities" in the Glass-Steagall Act by

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60 15 U.S.C. § 77b(1)(1976) (Securities Act); *id.* § 78c(a)(10) (Securities Exchange Act).

61 *ICI II*, *supra* note 22, 450 U.S. at 61 & n. 27, 101 S.Ct. at 984 & n. 27. *See generally supra* pp. 141-143 [230A-232A].

62 *United Housing Found., Inc.* v. *Forman*, 421 U.S. 837, 849, 95 S.Ct. 2051, 2059, 44 L.Ed.2d 621 (1975) (emphasis added).

63 The Supreme Court's recent interpretations of these provisions of the Glass-Steagall Act make no reference at all to the securities laws. *See generally ICI I*, *supra* note 37; *ICI II*, *supra* note 22.

64 *United Housing Found., Inc.*, 421 U.S. at 849, 95 S.Ct. at 2059 (emphasis added).

analyzing the economic policy behind the Act—to protect bank depositors from the hazards which ensue when commercial banks enter the investment banking business.[65] In short, the Glass-Steagall Act uses the term "security" to fence off investment banking activities from commercial banks; the securities laws use the term to define the capital markets whose economic functioning is to be regulated by the securities laws. Clearly, the scope of the term may differ in these differing contexts. We must assign the term "security" a different meaning in the Glass-Steagall and the Securities Acts if a different interpretation is called for by the respective policies of those Acts.[66]

The Supreme Court recently reaffirmed this approach to the Securities Acts in *Marine Bank* v. *Weaver*.[67] "The [Securities Exchange] Act was adopted to restore *investors' confidence in the financial markets*. . . . We have repeatedly held that the test [of whether an instrument is a "security"] 'is what character the instrument is given in commerce by the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect.' "[68] Therefore, "[e]ach transaction must be analyzed and evaluated on the basis of the content of

65 *See infra* p. 148 [242A-244A] & notes 72-76.

66 Appellees emphasize that, because Congress *defined* "security" in the Securities Act to include "any note," it must have intended "security" in the Glass-Steagall Act to mean the same thing. But all the example of the Securities Acts shows, of course, is that Congress is capable of using "securities" to include "all notes" when it clearly defines the term in that way. Indeed, the example of those Acts suggests that, if Congress had intended so sweeping a definition of "security" in the Glass-Steagall Act, it would have enunciated such a definition in the Act. *Cf. American Tobacco Co.* v. *Patterson*, U.S. at n. 6, 102 S.Ct. 1534,at 1539 n. 6, 71 L.Ed.2d 748 ("fundamental distinction" should not be imported into a statute unless Congressional intent is clearly expressed); *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 572, 99 S.Ct. 2479, 2487, 61 L.Ed.2d 82 (1979) ("when Congress wished to provide [remedy], it knew how to do so and did so expressly").

67 ___ U.S.___, 102 S.Ct. 1220, 71 L.Ed.2d 409 (1982).

68 *Id.* at ___, 102 S.Ct. at 1222 (emphasis added) (citations omitted).

the instruments in question, the purposes intended to be served, and the factual setting as a whole."[69]

In deciding that a certificate of deposit was not a security, *Marine Bank* noted two facets of the economics of these certificates: first, holders receive a fixed rate of interest rather than dividends based on profits; second, "[i]t is unnecessary to subject issuers of bank certificates of deposit to liability under . . . the federal securities laws since the holders of bank certificates of deposit are abundantly protected under federal banking laws."[70] In short, the Court focused on the potential economic gains and losses of the *investors*, who are the intended beneficiaries of federal securities regulation, in deciding whether the purposes of that regulation would be furthered by its application to the instrument in question. A different focus of analysis is called for under the Glass-Steagall Act, which aims at protecting the integrity of *banks* and the financial resources of *depositors* rather than *investors*.

We conclude that the meaning of the term "securities" under the securities laws is of little immediate relevance to the problem before us; rather, the example of these laws suggests the need for a careful economic analysis of the commercial paper market itself.

E. *Functional Analysis of Commercial Paper*

The language and the legislative history of the Glass-Steagall Act strongly suggest that commercial paper should be viewed as a loan rather than as a "security" for the purposes of the Act. However, as we have seen, neither the language nor direct evidence from the legislative history is decisive of the question before us. There is no foolproof formula by which we can decide whether the commercial paper marketed by Bankers Trust constitutes a "security." Rather, as the Board observed,

> a broad generic or literal reading of the term "security" would likely encompass a number of instruments that

69 *Id.* at ____, n. 11, 102 S.Ct. at 1225, n. 11.

70 *Id.* at ____, 102 S.Ct. at 1225.

> banks routinely deal with in the course of their business and would, consequently, be contrary to the basic purpose of the Act. On the other hand, a highly technical or formalistic approach might permit evasions of the mandate of Congress.[71]

Because neither the literal language of the statute nor other expressions of congressional intent available to us directly indicate whether commercial paper is a "security," it is necessary to conduct a "functional analysis" of Bankers Trust's commercial paper to resolve this question. The problem becomes whether classifying commercial paper as a "security" would further the policies of the Act. As the Board phrased this inquiry:

> [I]f a particular kind of financial instrument evidences a transaction that is more functionally similar to a traditional commercial banking operation than to an investment transaction, then fidelity to the purposes of the Act would dictate that the instrument should not be viewed as a security.[72]

In adopting this functional analysis, the Board followed the Supreme Court's reasoning in its recent cases construing the Glass-Steagall Act. In *Investment Company Institute* v. *Camp* (*ICI I*) the Court noted that

> Congress was concerned that commercial banks in general and member banks of the Federal Reserve System in particular had both aggravated and been damaged by stock market decline partly because of their direct and indirect involvement in the trading and ownership of speculative securities. The Glass-Steagall Act reflected a determination that policies . . . which might otherwise support the entry of commercial banks into the investment banking business were outweighed by the "hazards"

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71 Federal Reserve Statement, *supra* note 3, at 19, J.A. at 237.

72 *Id.*

and "financial dangers" that arise when commercial banks engage in the activities proscribed by the Act.[73]

Thus, if confronted with a banking practice which involves the sale of securities and for that reason threatens the "hazards" at which the Act is aimed, neither the Federal Reserve Board nor this court is free to "balance" these hazards against the perceived benefits of the proposed practice. If the practice does *not* threaten to cause these hazards, however, we need undertake no such balancing. Rather, we effectuate the will of Congress by concluding that the proposed banking practice is not within the scope of the statutory proscription.

For example, in *ICI I* the Court found that the bank's sale of participations in a bank-sponsored mutual fund posed the dangers that the Glass-Steagall Act was designed to prevent; the Court concluded that these participations were securities within the meaning of the Act.[74] Once these participations were found under this functional analysis to be "securities," the "literal language" of the Act prohibited sale by the bank.[75]

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73 *ICI I*, *supra* note 37, 401 U.S. at 629-30, 91 S.Ct. at 1098.

74 *Id.* at 635-38, 91 S.Ct. at 1101-02.

75 *Id.* at 639, 91 S.Ct. at 1103. *See also ICI II*, *supra* note 22, 450 U.S. at 65-66, 1-1 S.Ct. at 986 (analyzing *ICI I*) ("This Court's . . . determination [that the units of participation were securities] led inexorably to the conclusion that § 16 had been violated."). *ICI II* posed a different problem of statutory interpretation, as the Court itself noted. *Id.* at 66, 101 S.Ct. at 986. There, it was indisputable that the transactions under scrutiny involved "securities"; the question before the Court was whether the banks were "engaged in the business of issuing, underwriting, selling, or distributing" securities. Again, the Court embarked upon an analysis of the "hazards contemplated [by] Congress in enacting the Glass-Steagall Act" in order to conclude that the Act had not been violated. *Id.* at 66-67, 101 S.Ct. at 986-87.

Because we find that the commercial paper marketed by Bankers Trust is not a "security," we need not reach the issue, which arose in *ICI II*, of whether the bank is engaged in "underwriting" within the meaning of the Glass-Steagall Act.

The Federal Reserve Board, in resolving the present case, therefore correctly focused on whether the commercial paper marketed by Bankers Trust functioned economically as a loan or as a security. Only if commercial paper displayed the economic characteristics of a "security" would the marketing of commercial paper by Bankers Trust cause the hazards the Act was designed to prevent. The Board concluded that, in all relevant respects, the commercial paper had the economic characteristics of a loan.[76] We agree.

It is useful to review the traditional lending functions of commercial banks. The commercial lender extends *short-term* credit to businesses to finance immediate needs for working capital.[77] To assure itself of timely repayment, the commercial bank carefully evaluates the credit-worthiness of the borrower and the borrower's representations as to the use of funds. In recent years, the lender has characteristically been either a bank or a syndicate of lenders, which may include banks and lending institutions such as credit or mortgage companies.[78]

We find that the commercial paper at issue here has the economic characteristics of a traditional loan. Purchase of commercial paper, like lending by a commercial bank, represents a very reliable means by which the lender may earn a return on excess cash over a short period of time. Several features of the commercial paper market are salient in this respect.

First, the default rate on commercial paper is extremely low: only highly solvent corporations, with the best possible bond ratings, are able to market commercial paper. Indeed, the default rate on commercial paper is much lower than that on

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76 Statement, *supra* note 3, at 17-20, J.A. at 236-39.

77 *See, e.g.*, D. Hayes, Bank Lending Policies 89-91 (1977); J. Culbertson, Money and Banking 308-09 (2d ed. 1977). In considering the Glass-Steagall Act, Congress emphasized the distinction between short-term and long-term capital financing. *See supra* p. 145 [237A] & notes 52-53.

78 *See* Pollock, *Notes Issued in Syndicated Loans—A New Test to Define Securities*, 32 Bus. Lawyers 537, 538 (1977).

ordinary commercial loans made to high-grade commercial customers.[79]

Second, Bankers Trust commercial paper, like most commercial loans, is of very short maturity: it is generally redeemable at face value within 30 to 90 days.[80] Short maturity not only makes commercial paper a very liquid investment; it also reduces risk, because the financially strong corporations which can issue commercial paper are unlikely to deteriorate over the short period during which purchasers must hold the paper.

Third, because commercial paper is sold by Bankers Trust in denominations averaging one million dollars or more,[81] this paper is placed only with sophisticated purchasers—large institutions such as pension funds, money market mutual funds, insurance companies and nonfinancial corporations with large amounts of idle cash.[82] These purchasers, like commercial banks, are well able to evaluate the riskiness of the investments by verifying representations about the issuers. Three indepen-

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79 Federal Reserve Statement, *supra* note 3, at 3, J.A. at 222; Hurley, *supra* note 5, at 526-29. The Board's empirical studies found that the default rate on commercial paper is only a fraction of that on commercial loans. Companies which began to experience financial difficulties, such as Chrysler Financial Corp. and International Harvester Credit, must withdraw from the commercial paper market. Ironically, these corporations turn to commercial banks to meet their needs for current funding.

80 *See* Report from the Board's On-site Investigation of Bankers Trust 2 (8 May 1980) (average maturity of Bankers Trust notes 60 days), J.A. at 200 [hereinafter cited as Report]; Federal Reserve Statement, *supra* note 3, at 2, J.A. at 221. *See also* Hurley, *supra* note 5, at 530; Comment, *supra* note 5, at 364. According to a Federal Reserve Board survey, the maturities of short-term commercial and industrial loans range from 36 to 105 days. 67 Fed. Res. Bull. A26 (Dec. 1981).

81 *See* Report, *supra* note 80, at 2, J.A. at 200. The minimum denomination Bankers Trust will sell is $100,000.

82 Hurley, *supra* note 5, at 529; Comment, *supra* note 5, at 362-66.

dent rating services also conduct thorough periodic investigations of issuers' financial condition.[83]

For all these reasons, investment in commercial paper, far from resembling securities speculation, is less risky even than banks' ordinary commercial lending.[84] The key difference between the commercial paper sold by Bankers Trust and the traditional lending of commercial banks is that capital is lent by other investors rather than by the bank.[85] In the traditional loan transaction, the commercial bank *purchases* commercial paper; in the present case, the bank acts as agent in the *sale* of commercial paper. The bank is simply on the other side of the transaction. The question which faced the Board is whether commercial paper should be considered a "security" merely because the bank acts as the seller rather than the purchaser of the commercial paper—*i.e.*, whether the role of the bank in and of itself makes the transaction one prohibited by the Glass-Steagall Act.[86]

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83 *See* sources cited at note 82 *supra*.

84 Notably, securities differ strikingly from loans in all three respects. First, purchasers of securities, unlike purchasers of commercial paper, may liquidate their holdings, if at all, only at whatever price the market is currently paying for the stock. Second, because this price will fluctuate with the fortunes of the firm and with general economic conditions, holding securities is risky (though of course the degree of risk will depend on the profitability of the enterprise and the terms of the security agreement). Third, securities are generally available in much smaller denominations than commercial paper, so that they may be traded by the public on the open market.

85 Federal Reserve Statement, *supra* note 3, at 19, J.A. at 238. When Congress passed the Glass-Steagall Act, this difference was less marked than it has been in recent years: banks not only arranged loans in private transactions, but also purchased the vast bulk of instruments sold through the commercial paper market. *See id.* at 18, J.A. at 237; Hurley, *supra* note [illegible], at 529. *Compare supra* p. 148 [244A] & n. 78 (in commercial bank loan, lender may be either the bank itself or a syndicate of other lenders).

86 *See Becker*, 519 F. Supp. at 615-16.

We agree with the Board that Bankers Trust may sell as well as purchase commercial paper. The bank's role as seller does not threaten the bank with those dangers which the Glass-Steagall Act was designed to prevent. Because commercial paper is like a loan rather than a security, marketing of commercial paper by the bank does not have the same economic impact on the bank as would marketing of securities.

This is confirmed by an analysis of the dangers which the Glass-Steagall Act was designed to prevent.[87] One such danger was that bank underwriting of *securities* may "tie up" depositors' funds in speculative securities. Bankers Trust's sale of commercial paper does not create this danger because of the features of commercial paper already noted. First, the bank acts simply as an agent in the sale of commercial paper; it does not agree to purchase the paper on its own account—*i.e.*, with the funds of depositors.[88] Second, commercial paper is of prime quality, sold only by corporations with well-established credit ratings: commercial paper is not a "speculative" holding.[89] Third, commercial paper is held by the lender only for 30 to 90 days:[90] the lender may readily convert his holdings to cash and does not bear the risk of long-term fluctuations in the value of the enterprise.

The other set of dangers addressed by the Glass-Steagall Act comprises the conflicts of interest that arise when a commercial bank underwrites securities.[91] Again, Bankers Trust does not face these conflicts.

First, the bank cannot use its credit facilities in order to facilitate sale of its commercial paper. Because the interest on a commercial loan is higher than that paid out on commercial

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87 *See supra* pp. 141-43 [230A-232A].

88 Report, *supra* note 80, at 4, J.A. at 202; Federal Reserve Statement, *supra* note 3, at 2.

89 *See supra* pp. 148-149 [244A-246A].

90 *See supra* pp. 149 [245A-246A].

91 *See supra* pp. 142-143 [231A-232A].

paper, a purchaser of commercial paper would not use a commercial loan to finance its purchases.[92] Conversely, the bank is under no incentive to advance unsound loans to shore up its issuers of commercial paper, because these issuers must be, by the nature of the commercial paper market, financially sound.[93]

Second, Bankers Trust is not in a position to abuse its reputation for prudence, or give unreliable financial advice to its depositors, in order to promote the sale of commercial paper. Commercial paper is purchased only by large sophisticated buyers who are capable themselves of evaluating the wisdom of their investment.[94] Moreover, commercial paper is very low-risk, and is issued only by very solvent corporations about whose financial prospects information is widely available.[95] It is inconceivable that a commercial bank such as Bankers Trust could, under these conditions, seek improperly to influence potential purchasers of commercial paper.[96]

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92 *See* Guidelines, *supra* note 13, at 29334. *See also* Report, *supra* note 80, at 4, J.A. at 202 (no evidence that funds borrowed from Bankers Trust are used to purchase its commercial paper).

93 *See supra* pp. 148-149 [244A-246A].

94 *See supra* p. 149 [245A-246A].

95 *See supra* p. 148 [244A-245A].

96 Finally, Bankers Trust may not "dump" its commercial paper through its trust department, for the Federal Reserve Guidelines prohibit bank sales of commercial paper to fiduciary accounts to which the bank gives investment advice. *See* Guidelines, *supra* note 13, at 29335 (Guideline #7). Insofar as the conflict of interest presented here may be entirely eliminated by an authorized regulation of the Board, it can hardly be said to pose one of the "subtle hazards" against which the Act is directed. *ICI I*, *supra* note 37, 401 U.S. at 630, 91 S.Ct. at 1098. *See also ICI II*, *supra* note 22, 450 U.S. at 66-67, 101 S.Ct. at 986 (relying on Board guidelines in finding no "underwriting" by banks); *cf. Marine Bank*, ___ U.S. at ___, 102 S.Ct. at 1225 (regulation of certificates of deposit by securities laws unnecessary because of extensive federal banking regulation).

Finally, the bank's reputation for prudence will not suffer by its association with the issue of commercial paper. Commercial paper is a highly sound short-term investment. And even if a commercial paper issuer were to default, the sophisticated purchasers of commercial paper will understand that this paper is not backed by the guarantees on commercial bank deposits.

The Board's "functional analysis" leads inexorably to the conclusion that Bankers Trust's commercial paper is not a "security" within the meaning of the Glass-Steagall Act. Transactions in commercial paper display the key economic characteristics of a commercial bank loan; and, because of these characteristics, Bankers Trust's dealings in commercial paper pose none of the hazards the Glass-Steagall Act was designed to prevent.

IV. CONCLUSION

We thus agree with the Board that Bankers Trust may continue to deal in commercial paper without violating the Glass-Steagall Act. The commercial paper it markets is not a "security" within the prohibitions of the Act. Moreover, our reasoning applies to other commercial paper which falls within the Board's guidelines—*i.e.*, prime quality commercial paper, of maturity less than nine months, sold in denominations of over $100,000 to financially sophisticated customers rather than to the general public.[97] Commercial banks which deal in this paper are not subject to the risks which the Glass-Steagall Act was designed to prevent. We hold therefore that commer-

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97 *See* Guidelines, *supra* note 13, at 29334 (Guideline # 1). The Board's Guidelines, in addition to defining permissible types of commercial paper and permissible purchasers and sellers, require forms of disclosure, record-keeping, and credit analysis by commercial banks. *See supra* p. 8. These requirements are directed against the danger that sale of third-party commercial paper might involve "unsafe or unsound [banking] practices." In finding that the transactions regulated by the Guidelines do not involve a sale of *securities*, we do not rely on these additional requirements.

cial banks may sell third party commercial paper provided that they comply with the Board's guidelines.

It is appropriate to note, however, the limits to this holding. It is conceivable that another type of commercial paper—*e.g.*, of smaller denominations, or issued to the general public—might be a "security" under the Glass-Steagall Act. Commercial bank involvement in the market for such commercial paper may well undermine bank solvency or create unavoidable conflicts of interest. Moreover, the present case does not require us to decide whether Bankers Trust is engaged in "underwriting." A commercial bank is permitted to underwrite commercial paper so long as commercial paper is not a "security." If other species of commercial paper prove to be a "security," however, the issue what constituted "underwriting" of commercial paper would then have to be decided.

Our opinion does not touch directly on other species of commercial paper. As the commercial paper market and banking practices continue to evolve, the Board will be called upon to determine in varying fact situations the scope of activities that Congress intended to permit banks to undertake. But these hypothetical situations are irrelevant to the problem before us. Because the Board correctly applied its functional analysis to the instant case, the judgment of the district court is *Reversed*.

ROBB, *Senior Circuit Judge*, dissenting:

I dissent. In my opinion the majority's holding contravenes the fundamental policy of the Glass-Steagall Act. That Act seeks to insulate commercial banking from the hazards inherent in investment banking by mandating a complete separation of those two functions. The majority decision violates this separation of functions by finding no difference under the Act between a lender in a commercial loan transaction and a seller in the sale of third-party commercial paper.

Although offering various justifications, the majority ultimately rests its holding on a "functional analysis" of Bankers

Trust's third-party commercial paper sales. In its functional analysis, the majority dismisses the difference between the bank's role as "purchaser" in a commercial loan transaction and its role as "seller" in a third-party commercial paper transaction as a case of the bank "simply [being] on the other side of the transaction." *Ante* at 150 [27a]. This distinction, however, is determinative under the Act. Through the Act Congress sought a complete separation of commercial banking from investment banking. *See Investment Co. Institute* v. *Camp*, 401 U.S. 617, 629, 632, 91 S.Ct. 1091, 1098, 1099, 28 L.Ed.2d 367 (1971). *See also Board of Governors of Federal Reserve System* v. *Investment Co. Institute*, 450 U.S. 46, 62, 101 S.Ct. 973, 984, 67 L.Ed.2d 36 (1981). The critical distinction between commercial banking and investment banking is the bank's role in the transaction.

When a bank lends money it is the investor. Following a thorough credit analysis of the potential borrower, the bank decides whether to approve the loan. A loan that the bank has approved and funded constitutes an asset of the bank for which the bank has placed its funds at risk. The bank's generation of income and collection of principal are dependent on the wisdom of the bank's credit decision, the adequacy of the loan provisions, and the bank's perseverance in collecting the loan.

In contrast, when a bank markets third-party commercial paper, it is the seller, not the investor. As seller, the bank has less incentive to conduct a thorough credit analysis of the commercial paper issuer because the bank, unlike an investor, does not place its funds at risk. The bank earns its fee upon closing the sale of the commercial paper. Once the sale is complete, the bank has no direct financial interest in the issuer's ability to meet its commercial paper obligations.

Ignoring the differences in the bank's roles as lender and as seller, the majority characterizes commercial loans as "short-term" transactions and then avers that selling commercial paper is no different than making a commercial loan because both transactions have short maturities. *Ante* at 143-144 [244A-246A]. This analysis fails for two reasons. First, any

interpretation of the Act must focus on the bank's role in the transaction with a view to maintaining the Act's separation of banking functions. The majority's focus on maturities provides no help in determining whether the bank's role in the transaction violates the Act. Second, the basic premise of the majority's analysis is incorrect. Commercial lending is not limited to short-term loans. Longer maturity loans for the acquisition of fixed assets and for permanent increases in working capital are important commercial lending services which the majority conveniently ignores. *See* D. Hayes, *Bank Lending Policies*, 89, 107, 109 (2d ed. 1977); G. Munn, *Encyclopedia of Banking and Finance* 892 (7th ed. 1973). *See generally Business Loans of American Commercial Banks* chs. 7, 9 (B. Beckhart ed. 1959).

Similarly, an analogy between commercial paper sales and commercial loans, based on low default rates and the sophistication of the investors, *ante* at 144 [25a-27a], is not helpful. Relying on these factors, a bank could transform "transactions unquestionably at the heart of the securities industry into permissible activity for commercial depository banks." *A.G. Becker, Inc.* v. *Board of Governors of the Federal Reserve System*, 519 F.Supp. 602, 615 (D.D.C. 1981).

The majority says that analysis of the hazards of mixing commercial and investment banking "confirms" the result reached through its functional analysis. I reach the opposite conclusion. In *Investment Co. Institute* v. *Camp*, 401 U.S. 617, 91 S.Ct. 1091, 28 L.Ed.2d 367 (1971), the Supreme Court lists several hazards that arise when commercial banks become peddlers of securities. First, commercial banks may suffer losses from imprudent security investments. *Id.* at 630, 91 S.Ct. at 1098. Second, "the bank's salesman's interest might impair its ability to function as an impartial source of credit." *Id.* at 631, 91 S.Ct. at 1099. Third, commercial banks may lose customer good will if their depositors suffer losses on investments made in reliance on the bank's involvement in the transaction. *Id.* Fourth, commercial banks may use their reputation for prudence to further their securities sales and subject that reputation to the risks necessarily incident to the investment banking business. *Id.* at 632, 91 S.Ct. at 1099. Finally,

the bank's promotional interests could conflict with its commercial banker obligation to render disinterested investment advice. *Id.* at 633, 91 S.Ct. at 1100.

The majority makes short work of the hazards discussed in the *Camp* decision. Those hazards, in the majority's view, are irrelevant here because commercial paper is a "prime quality", "very low-risk" investment, issued by "financially sound" issuers, and sold to "sophisticated" investors. *Ante* at 150-151 [28a-30a]. The majority's self-fulfilling analysis misses the point. "Prime quality" and "very low-risk" are characterizations that are justified only after an investment has been terminated without any investor loss. The drafters of the Act were certainly more wary of such characterizations in 1933 than the majority is today. The Act has no provision permitting bank sales of securities which are "prime quality" or "very low-risk".

To determine whether the bank's sale of third-party commercial paper involves the hazards that the Act seeks to prevent, we must take the perspective of the Act's drafters. The recent Penn Central experience provides such a perspective. *See generally* Staff of Securities & Exchange Commission, 92d Cong., 2d Sess., *Report to Special Subcomm. on Investigations of the House Comm. on Interstate and Foreign Commerce, The Financial Collapse of the Penn Central Company* (Subcomm. Print 1972) [hereinafter cited as *Penn Central Report*]. As a consequence of its bankruptcy on June 21, 1970 the Penn Central Transportation Company defaulted on $82.5 million in commercial paper. *Id.* at 1. Goldman, Sachs & Co., the nation's largest commercial paper dealer, had sold the commercial paper during the seven months preceding the bankruptcy. *Id.* at 290. The National Credit Office, a wholly-owned subsidiary of Dun & Bradstreet, Inc., had given Penn Central's commercial paper its highest rating, "prime", until June 1, 1970. *Id.* at 283. The investors, whom Goldman, Sachs & Co. described as "sophisticated" and "capable of making their own investment decisions," had purchased Penn Central commercial paper in $100,000 denominations. *Id.* at 290.

A review of the *Camp* warnings in light of the Penn Central experience presents a picture very different from that which the

majority draws. First, although Bankers Trust makes no commitment to purchase unsold commercial paper, it makes clear in its promotional letter to commercial paper issuers that such purchases are within the ambit of its investment services.

> However, in those rare occasions in which we would be unable to satisfy all of [the issuer's] requirements through the placement of paper with investors, we may, from time-to-time and without prior commitment, lend [the issuer] money at the commercial paper rate, and take back a commercial paper note.

(J.A. at 61). *See also* J.A. at 27, 50. The majority states that bank purchases of commercial paper would not present a problem because commercial paper is "prime quality, [is] sold by corporations with well-established credit ratings," and is a short-term investment. *Ante* at 150 [274A-279A]. Yet a bank's purchase of Penn Central's commercial paper which fit the majority's criteria just three weeks before it became worthless, would have been a perfect example of the hazard of "imprudent investment" that the Act seeks to prevent.

Second, the majority states that commercial paper issuers are "financially sound" companies and, therefore, have no need for commercial loans to strengthen their financial position. *Ante* at 150-151 [274A-279A]. However, as the Penn Central case demonstrates, commercial paper issuers are not exempt from financial difficulties. A bank's interests in handling the issuer's commercial paper sales and in protecting the bank's reputation for sound financial decisionmaking could "distort" its credit decisions or lead to unsound loans" to issuers for whom the bank regularly sells commercial paper. *Investment Co. Institute* v. *Camp*, 401 U.S. at 637, 91 S.Ct. at 1102.

The third hazard discussed in the *Camp* decision arises when a bank sells third-party commercial paper under any circumstances less idealistic than those which the majority envisions. Bank depositors who are financially able to purchase commercial paper in large denominations are likely to be among the bank's most important and influential clientele. Loss of their good will as a result of losses on investments which the bank

recommended and sold could be detrimental to the bank's commercial operations.

Finally, the majority makes the indisputable statement that when a bank sells "very low-risk" commercial paper of "very solvent" corporations to "large, sophisticated" investors the bank is not in a position to abuse its reputation for prudence or to give unreliable financial advice. *Ante* at 150 [247A-249A]. However, commercial paper sales that initially fit the majority's criteria may, before the investors are repaid, create hazards that the Act seeks to prevent.

Goldman, Sachs & Co. sold $5 million of the commercial paper of Penn Central, the nation's fourth largest corporation, to American Express Company, a sophisticated investor, on May 1, 1970. *Penn Central Report* at 286, 291. That sale, following several indications of major problems at Penn Central, *id.* at 279-86, and preceding the Company's collapse by just seven weeks, demonstrates the hazards present when there is a financial incentive to give unreliable advice. Had Bankers Trust been Penn Central's securities peddler, the association with Penn Central's collapse together with the resulting lawsuits which the bank would have had to defend would have severely damaged the bank's reputation for financial prudence. *See* Comment, *The Commercial Paper Market and the Securities Acts*, 39 U.Chi.L.Rev. 362, 378-79 nn. 112-13 (1972).

We must analyze the Act with the intent of its drafters as our guide. The Act was a "drastic step", *Investment Co. Institute* v. *Camp*, 401 U.S. at 629, 91 S.Ct. at 1098, taken during a bleak period in our country's banking history. Its drafters intended a complete separation of commercial banking from investment banking without regard to the likely "soundness" of the securities which a bank might sell. Senator Bulkley stated this uncompromising position at the time of the Act's passage: "If we want banking service to be strictly banking service, without the expectation of additional profits in selling something to customers, we must keep the banks out of the investment security business." *Investment Co. Institute* v. *Camp*, 401 U.S. at 634, 91 S.Ct. at 1100 (quoting 75 Cong. Rec. 9912 (1932) (remarks of Sen. Bulkley)). Permitting a bank

to sell third-party commercial paper presents the same hazards that "Congress determined . . . made it necessary to prohibit . . . [investment banking] activity to commercial banks." *Investment Co. Institute* v. *Camp*, 401 U.S. at 636, 91 S.Ct. at 1101. As a result, we must look closely to determine whether the Act prohibits banks from selling third-party commercial paper.

Unlike the majority, I find the Act's language helpful in determining whether commercial paper is a "note" or "security". For our purposes the Act raises two issues. The first issue is whether commercial paper is an instrument with which the Act is concerned—"stocks, bonds, debentures, notes, or other securities," 12 U.S.C. § 378(a)(1) (1976). The second issue is whether Bankers Trust is engaged in the "issuing, underwriting, selling, or distributing," *id.*, activities which the Act prohibits.

The majority characterizes the terms "stocks", "bonds", "debentures", and "notes" as "specific type[s] of long-term investment securit[ies]." *Ante* at 143-144 [234A]. The majority concludes that a broader definition of the term "notes" would be inappropriate because it would include instruments such as commercial paper "which have little in common with these long-term investment securities." *Ante* at 144 [234A]. The majority's reliance on maturities to force a narrow meaning onto the terms of the Act is misplaced. The Supreme Court has interpreted the Act's terms broadly.

> [N]othing in the phrasing of either § 16 or § 21 . . . suggests a narrow reading of the word "securities." To the contrary, the breadth of the term is implicit in the fact that the antecedent statutory language encompasses not only equity securities but also securities representing debt.

Investment Co. Institute v. *Camp*, 401 U.S. at 635, 91 S.Ct. at 1101. *See also Board of Governors of Federal Reserve System* v. *Investment Co. Institute*, 450 U.S. at 65, 101 S.Ct. 986. The terms "stocks", "bonds", "debentures", and "notes" have broad meanings which encompass a multitude of different instruments. The term "other securities" further indicates the

breadth of the Act's coverage; it catches any instruments which are not otherwise defined by the prior four terms. Taken as a group these five terms cover the spectrum of instruments which a corporation might seek to market. Relying "squarely on the language . . . of the Glass-Steagall Act," *Board of Governors of Federal Reserve System* v. *Investment Co. Institute*, 450 U.S. at 65, 101 S.Ct. at 986. I would find that commercial paper is a type of instrument with which the Act is concerned.

Although analysis of the Act's terms and of the hazards with which the Act is concerned requires a finding that commercial paper is a "note or other security" under the Act, our inquiry is not complete. There remains the second issue of whether Bankers Trust's commercial paper sales is an activity which the Act prohibits. However, neither the Federal Reserve Board nor the District Court reached this second issue. *A.G. Becker Inc.* v. *Board of Governors of Federal Reserve System*, 519 F. Supp. 602, 616 n. 10 (D.D.C. 1981). Therefore the second issue is not before us on this appeal.

I would affirm the District Court's finding that commercial paper is a "note or other security" under the Act, and would remand this case for the further determinations suggested in this dissent.

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 80-2258, 81-1493, 81-2070, 81-2096,
80-2314 and 81-2058

February 2, 1983

A.G. BECKER INCORPORATED,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Respondents.

SECURITIES INDUSTRY ASSOCIATION,

Petitioner,

—v.—

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM, et al.,

Respondents.

Before:

TAMM and WILKEY, *Circuit Judges,*
and ROBB, *Senior Circuit Judge.*

ORDER

On consideration of the joint petition for rehearing of A.G. Becker, Inc. and the Securities Industry Association, filed December 17, 1982, it is

ORDERED by the Court that the aforesaid petition is denied.

Per Curiam

For The Court

GEORGE A. FISHER, *Clerk*

By: Robert A. Bonner
Chief Deputy Clerk

Senior Circuit Judge Robb did not participate in the foregoing order.

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Before:

ROBINSON, *Chief Judge,* WRIGHT, TAMM,
MACKINNON, WILKEY, WALD, MIKVA, EDWARDS, GINSBURG,
BORK and SCALIA, *Circuit Judges.*

ORDER

The joint suggestion for rehearing *en banc* of A.G. Becker, Inc. and the Securities Industry Association has been circulated to the full Court. A majority of the Court has not voted in favor thereof. On consideration of the foregoing, it is

ORDERED by the Court *en banc* that the aforesaid suggestion is denied.

Per Curiam

For The Court

GEORGE A. FISHER, *Clerk*

By: Robert A. Bonner

Circuit Judges MacKinnon and Mikva would grant the suggestion for rehearing *en banc*.

Chief Judge Robinson and Circuit Judges Wald, Ginsburg and Bork did not participate in the foregoing order.